# SUPREME COURT OF THE UNITED STATES

## OCTOBER TERM, 1933

# No. 114

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THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL., APPELLANTS,

*vs.*

THE WICHITA GAS COMPANY, THE HUTCHINSON GAS COMPANY, THE NEWTON GAS COMPANY, ET AL.

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APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF KANSAS

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[fol. 5]

## IN UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS, FIRST DIVISION

In Equity. No. 1637-N

THE WICHITA GAS COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS and Jesse W. Greenleaf, Thurman Hill, and C. W. Campbell, as Members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, Defendants

**Bill of Complaint**—Filed Sept. 19, 1933

Comes now the Wichita Gas Company, a corporation, and alleges:

1

That it is a corporation duly organized and existing under the laws of the State of Kansas, with its principal office, place of business and post office address at Wichita, in said state.

[fol. 6] 2

That the Public Service Commission of the State of Kansas is a legislative and administrative body created by the laws of the State of Kansas, having its office and principal place of business in the City of Topeka, Kansas, and is within the jurisdiction of this court. The defendants, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, at all times complained of herein have assumed to act as members of said Commission; that Roland Boynton is the duly elected and acting attorney general of the State of Kansas.

3

That the plaintiff is a resident and citizen of the State of Kansas and each and all of the defendants are residents

and citizens of the State of Kansas. The amount in controversy herein is more than $3,000.00 exclusive of interest and costs.

4

That this is a suit in equity arising under and involving the construction and application of the Constitution and Laws of the United States in that plaintiff is herein seeking to have permanently enjoined certain orders of the Public Service Commission of the State of Kansas, issued August 31st, 1932, for the reason that the same are unconstitutional, null and void because repugnant to the Fourteenth Amendment to the Constitution of the United States and the First Sub-Division of Section 10 of Article 1 of the Constitution of he United States, Clause 3, Section 8, Article 1 of the Constitution of the United States, in that said orders deprive plaintiff of its property without due process of law, [fol. 7] deny it the equal protection of the law, impair the obligation of its contracts, undertake to legislate with respect to interstate commerce and usurp the business management of plaintiff company.

5

That plaintiff is engaged in the business of distributing and selling natural gas for all purposes in Wichita, Kansas, and vicinity and is a public utility under the jurisdiction of said defendant Commission.

6

That plaintiff does not produce or manufacture gas and has no supply for sale and distribution to its customers other than the supply it purchases from the Cities Service Gas Company at the agreed price of forty (40) cents per thousand cubic feet for domestic purposes; that said Cities Service Gas Company refuses to sell domestic gas to plaintiff for a less price and plaintiff has no other source of supply available to it, and without its present supply cannot carry on its said business.

7

That the present value of plaintiff's property used and useful in rendering the service in which it is engaged is not less than the sum of $2,872,854.00; that it is operating under

the jurisdiction of said Commission and is charging for all gas sold by it for domestic purposes rates heretofore es-
[fol. 8] tablished and approved by said Commission; that under said existing rates its net earnings for the year ending June 30th, 1932, were $181,096.00, which constitutes an earning of only 6.3 per cent on the present fair value of its property for return and depreciation and which earning is unreasonably inadequate and confiscatory.

8

That notwithstanding the experience of plaintiff under existing rates and the inadequacy and unreasonableness of its present earnings, said defendant Commission under date of July 2nd, 1931, on its own motion issued an order in its docket number 13127 entitled, "In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company," by the terms of which it ordered this plaintiff and nine other corporations engaged in the sale and distribution of natural gas in approximately one hundred cities and communities in the State of Kansas to appear and furnish to the Commission such evidence as they might desire or the Commission might require as to the reasonableness of certain contracts. A full, true and correct copy of said order is hereto attached, marked Exhibit "A," and made a part hereof.

9

That pursuant to said order, Exhibit "A," plaintiff appeared specially before said Commission and objecting to the jurisdiction of the Commission; filed its special appearance, a full, true and correct copy of which is hereto attached, marked Exhibit "B," and made a part hereof.

[fol. 9] 10

That from the date of the issuance of said order, Exhibit "A," up to and including February 16th, 1932, numerous hearings were had before said Commission in which evidence was introduced by this plaintiff, by the other respondents to said proceeding, and by expert witnesses, engineers and accountants employed for the special purpose by said Commission itself.

11

That on July 20th, 1932, said Commission handed down its opinion, findings and order in said proceeding, a full, true and correct copy of which is filed herewith, marked Exhibit "C," and made a part hereof, the same being too voluminous to attach hereto.

12

That by said opinion, findings and order said Commission undertook to find unreasonable the contract between plaintiff and Henry L. Doherty & Company and undertook to order plaintiff to discontinue the setting up on its books of any payments due or to become due thereunder and to dicontinue making any such payments; undertook to find that the contract between plaintiff and the Cities Service Gas Company, under which it purchases its entire supply of gas for distribution in its said business, was unreasonable and undertook to order plaintiff to discontinue setting up on its books any payments due under said contract or to make any such payments, and undertook to order plaintiff to make no payments to said Cities Service Gas Company for gas so purchased in excess of Twenty-nine and One-half (29½c) Cents per thousand cubic feet, hereinafter [fol. 10] called M. C. F., notwithstanding the fact that the contract between plaintiff and said Cities Service Gas Company requires the payment of 40 Cents per M. C. F. for all gas so purchased; and undertook to order plaintiff to reduce its rates to all its domestic customers in proportion to the reduction in expenses brought about by the attempted reduction in the price of purchased gas, pending a final determination as to what proper rates for plaintiff should be.

13

That being dissatisfied with said opinion, findings and order, plaintiff on July 30th, 1932, and within the time provided by law, filed with said Commission its application for a rehearing as required by law, a full, true and correct copy of which application is hereto attached, marked Exhibit "D," and made a part hereof.

14

That on August 5th, 1932, said application was by said Commission allowed as to paragraph 39 thereof and denied

as to the matters, reasons and grounds set out in the remaining 50 paragraphs of said application. A full, true and correct copy of said order granting a rehearing is hereto attached, marked Exhibit "E," and made a part hereof.

15

Pursuant to said order granting a rehearing, Exhibit "E", said Commission reopened said proceedings and set the same for further hearing on August 15th, 1932, at which time plaintiff appeared and introduced evidence as [fol. 11] to the earnings of the Cities Service Gas Company for the year ending June 30th, 1932, which was received by said Commission.

16

That on said rehearing so had on August 15th, 1932, plaintiff attempted to introduce other evidence in connection with other matters assigned and alleged as grounds for a rehearing in said application, Exhibit "E," but was wrongfully and unlawfully denied the right so to do, said Commission informing plaintiff that said rehearing was as to the allegations of paragraph 39 of plaintiff's said application, Exhibit "E," only, and that no evidence as to other matters alleged in said application, or relevant to other issues or features of said proceeding would be heard by said Commission, notwithstanding the contention of plaintiff and the fact that the Commission was without jurisdiction to grant a partial rehearing, and that plaintiff's application having been granted said proceedings were open for all purposes of the original hearings.

17

That upon the refusal of said Commission to permit witnesses to be sworn or testimony introduced concerning matters other than those alleged in paragraph 39 of plaintiff's said application, Exhibit "E," and the unlawful and wrongful denial by said Commission of plaintiff's right to introduce other evidence, plaintiff formally made offers to introduce evidence showing:

(a) That the present fair value of its property used and useful in rendering service to its consumers in the City of

Wichita, Kansas, was $2,872,854; that its gross earnings [fol. 12] for the year ending June 30th, 1932, were $1,818,850; that its net earnings applicable to depreciation and return for said period were $181,096; that if present salary reductions had been in effect for said entire period net earnings applicable to depreciation and return would have been $205,434, or 7.2 per cent on the present fair value of its property; that it could not purchase gas for domestic purposes for less than 40 cents per M. C. F. and that the reduction in plaintiff's rates attempted to be ordered in the Commission's order of July 20th, 1932, was unreasonable, unjust and would result in the confiscation of its property. A full, true and correct copy of said offer is hereto attached, marked Exhibit "F," and made a part hereof.

(b) That the gas reserves of the Cities Service Gas Company are not excessive and in the opinion of the officers of the company are necessary in order to guarantee service; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas Panhandle field was 1,263,000,000 cubic feet per day, of which only 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oil or blown in the air, and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that [fol. 13] said Commission now has under consideration an order limiting all takes from wells to 5 per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,267 acres allowed by this Commission will be wholly inadequate for even the coming winter and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commisson, service will fail; that under present practices in Texas the owners of approximately 10 per cent of the leases are producing approximately 82 per cent of the gas, none of which is connected to pipe lines or used by them; that rock pressure in certain areas has diminished from the original 430 pounds

to less than 50 pounds; that the gas in the area, including the 71,267 acres allowed by the Commission, is migrating to the low pressure area and will be lost to the pipe lines; that none of the gas reserves now owned and held by the Cities Service Gas Company was bought or is being held for speculation and that the Commission overestimated the amount of gas available to the Cities Service Gas Company from the 71,267 acres found by it to be sufficient. A full, true and correct copy of said offer is hereto attached, marked Exhibit "G," and made a part hereof.

(c) That the dry hole allowance of $12,000.00 per year fixed by said Commission in its order is wholly insufficient, unjust and unreasonable for the reason that in 1930 Cities Service Gas Company drilled ten dry holes at a cost of $174,748.00 and in 1931 drilled two dry holes at a cost of $126,339.00, and that it is impracticable to undertake any exploratory drilling with a limitation of $12,000.00 on the cost. A full, true and correct copy of said offer is hereto attached, marked Exhibit "H," and made a part hereof.

[fol. 14] (d) That the assumptions made by the Commission in its opinion, findings and order were not warranted in that rotary drilling is not generally used for gas wells in the fields where the wells of the Cities Service Gas Company are located and the expense of rotary drilling is greater than the cost of wells drilled with standard tools, all for the purpose of showing that the value found by the Commission of the gas wells of the Cities Service Gas Company was unreasonably low. A full, true and correct copy of said offer is hereto attached, marked Exhibit "I," and made a part hereof.

(e) That the present value of the property of all of the respondents (this plaintiff and nine other companies) in all of the cities served by them is $15,326,298.00; that their joint gross earnings for the year ending June 30th, 1932, were $7,092,398.00; that their net earnings applicable to depreciation and return for the same period were $665,233.00 subject to minor adjustments, and that had the present salary reductions been in effect for the entire period the net earnings would have been $756,989.00, or 4.9 per cent on the fair value of all of their properties. A full, true and correct copy of said offer is hereto attached, marked Exhibit "J," and made a part hereof.

18

That on August 31st, 1932, said Commission handed down its opinion on rehearing in which it added to the value of the property of the Cities Service Gas Company found by it as of September 1st, 1931, in its original opinion and findings, Exhibit "C," the sum of $119,275.00, and found said value to be as of September 1st, 1931, $73,148,510.00; that the net income of the Cities Service Gas Company for the year ending June 30th, 1932, amounted to [fol. 15] $7,861,516.85; that an item of $52,297.13 in the operating expenses of the Cities Service Gas Company representing payments made to Henry L. Doherty & Company should be disallowed; that an item of $50,000.00 in the operating expenses of the Cities Service Gas Company representing its expense in the proceedings before the Commission should be disallowed; that with both of said items deducted the net income before allowance for depreciation and depletion of the Cities Service Gas Company was the sum of $7,963,813.00; that allowances should be made for depreciation, depletion, amortization and dry hole expense aggregating $1,977,591.00; and that after such deductions the net income of the Cities Service Gas Company was for the year ending June 30th, 1932, $5,986,222.00, which the Commission finds is more than 8 per cent of the fair value of the property of the Cities Service Gas Company on September 1st, 1931, of $73,148,510.00, so found by said Commission (the exact percentage being 8.1837 per cent, and without the elimination of said item of $52,297.13, representing payments made to Henry L. Doherty & Company, and said item of $50,000.00, representing the expense of the proceding before said Commission, said percentage would have been 8.0438). A full, true and correct copy of said opinion on rehearing is hereto attached, marked Exhibit "K," and made a part hereof.

19

That in said opinion on rehearing, Exhibit "K," after finding the value of the property of the Cities Service Gas Company and the fact that during the year ending June 30th, 1932, it earned according to its actual experience only 8.0438 per cent on the value found by the Commis- [fol. 16] sion itself, and ignoring the fact that it had no

jurisdiction over the Cities Service Gas Company to fix its rates to be charged in interstate commerce, and ignoring the fact that it had under consideration only the reasonableness of the contract between the Cities Service Company and this plaintiff as of the time of said investigation, said Commission unlawfully and arbitrarily proceeded to find the average value of the property of the Cities Service Gas Company over a three year period, and the average depreciation and depletion requirements of said company over said period, and the average net income of the company over said period and in such manner arrived at the conclusion that a rate of 30 cents per M. C. F., if charged by the Cities Service Gas Company during said three year period, would have produced a return of 7 per cent on the average value of the property of said company during said period (the actual percentage being 6.98 per cent), all of which is pure speculation and conjecture and has no relevancy to the reasonableness or unreasonableness of said city gate contract at the present time.

20

That on the 31st day of August, 1932, and at the same time said Commission handed down its opinion on rehearing, it also issued an order directed to this plaintiff and to thirteen other companies joined with this plaintiff in said proceding in which it found that the contract between Henry L. Doherty & Company and this plaintiff under which this plaintiff pays to Henry L. Doherty & Company for services rendered by it one and three-fourths per cent of its gross revenues is unreasonable; that the contract between this plaintiff and the Cities Service Gas Company [fol. 17] under which it pays 40 cents for gas sold and delivered to it for domestic purposes is unreasonable in so far as it exceeds the 30-cent rate established by the Commission, and ordered that on and after September 1st, 1932, this plaintiff and all other respondents in said proceeding cease to set up on their books as an expense item any payment to Henry L. Doherty & Company under said contract requiring the payment of 1¾ per cent of their gross income or any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F. and that this plaintiff and its co-respondents in said proceeding before the Commission should give no

consideration to any such payments in fixing a rate for domestic consumers; that on October 17th, 1932, this plaintiff and its co-respondents in said proceeding before the Commission appear before said Commission and show cause why the reduction in expenses as set forth in said order should not be passed on to consumers with such other reductions as might be found reasonable. A full, true and correct copy of said order is hereto attached, marked Exhibit "L," and made a part hereof.

21

That on August 31st, 1932, and at the same time said Commission handed down its said opinion on rehearing, Exhibit "K," and its said order, Exhibit "L," and notwithstanding the fact that in said order, Exhibit "L," this plaintiff was ordered and directed to appear before said Commission on October 17th, 1932, and show cause why the reduction in its expenses occasioned by the elimination of the payment to Henry L. Doherty & Company and the reduction in the payment to the Cities Service Gas Company for gas purchased at the city gate should not be [fol. 18] passed on to its consumers, said Commission issued an order effective September 1st, 1932, and until a hearing is held and an order issued, that this plaintiff and its co-respondents in said proceeding before the Commission should charge rates to their respective consumers which would pass on to the consumers the different between what this plaintiff and its co-respondents in said proceeding are now paying the Cities Service Gas Company for gas at the city gate and the rate of 30 cents per M. C. F. found by said Commission. A full, true and correct copy of said order is hereto attached, marked Exhibit "M," and made a part hereof.

22

That on the 8th day of September, 1932, this plaintiff filed with said Commission its application for a rehearing, a full, true and correct copy of which application is hereto attached, marked Exhibit "N," and made a part hereof, and on September 9, 1932, filed a supplemental application for rehearing, hereto attached and marked Exhibit "O."

23

That said application and supplemental application for a rehearing, Exhibits "N" and "O," were by said Commission on the 12th day of September, 1932, denied.

24

That the orders so issued by said Commission on August 31st, 1932, Exhibits "L" and "M" hereto attached, in which said Commission finds unreasonable and refuses to recognize plaintiff's contract with Cities Service Gas Com- [fol. 19] pany for the purchase of its supply of gas at the city gate, its contract with Henry L. Doherty & Company under which plaintiff pays 1¾ per cent of its gross revenue for services rendered to it by said Henry L. Doherty & Company and said order purporting to put in effect as of September 1st, 1932, a reduction in rates of plaintiff on account of the disallowance by said Commission of items of its operating expense caused by the disapproval of said contracts, are unlawful, unreasonable and void because in direct violation of the Constitution and Laws of the State of Kansas and the Constitution and Laws of the United States, as hereinafter specified.

25

Contract with Cities Service Gas Company

That said orders of said Commission, and each and all of them, in so far as they purport to disapprove the contract entered into between plaintiff and the Cities Service Gas Company under the terms of which plaintiff pays to said Cities Service Gas Company the price of 40 cents per M. C. F. for gas sold and delivered to it at the city gate for domestic purposes and in so far as they and each of them purport to disallow as an item of plaintiff's operating expense any sum paid for purchased gas in excess of 30 cents per M. C. F., are unlawful, unreasonable, arbitrary and void for the following reasons:

(a) For the reason that in said opinions, findings and orders said Commission found the value of the property or rate base of the Cities Service Gas Company to be $73,148,510.00; that the earnings of said company for the year

ending June 30th, 1932, were $7,963,813.00 applicable to replacement reserves and return on the fair value of the [fol. 20] property; that replacement reserves for said period should be $1,977,591.00 and that the net income after reserves applicable to return on the value of said property was $5,986,222.00, which amounts to an earning of only 8.1837 per cent on said Commission's own rate base so found and said Commission's own allowance for replacement reserves, and an earning of only 8.0438 per cent if the sum of $52,297.13 wrongfully and unlawfully disallowed by said Commission as an item of operating expense on account of it being paid to Henry L. Doherty & Company and if the item of $50,000.00 wrongfully and unlawfully disallowed by said Commission as an item of operating expense for the reason that it represented expenses incurred in said proceedings before said Commission be included in expenses. And plaintiff alleges that said earning is less than a reasonable rate of return for said Cities Service Gas Company considering the unusual hazards of its business and is less than a return necessary to attract capital to said business at this time and under present conditions, it therefore being apparent on the face of said opinions, findings and orders that the contract between plaintiff and the Cities Service Gas Company is reasonable, does not indicate any absence of arm's length dealing between plaintiff and said company on account of their affiliation and should not have been disapproved.

(b) For the reason that the attempt of said Commission in said opinions, findings and orders, and each of them, to avoid the clear and undisputed reasonableness of the earnings of the said Cities Service Gas Company by averaging the earnings over a period of years and applying same to an average value of property, is unreasonable, unjust and unlawful and does not change or alter the Commission's finding that said Cities Service Gas Company [fol. 21] earned only 8.1837 per cent on the value of its property found by said Commission after deducting reserves approved by said Commission, said Commission having no jurisdiction, power or authority to determine the present reasonableness or unreasonableness of said contract on the property values and earnings of said Cities Service Gas Company as of any time other than the time said opinions, findings and orders were entered.

(c) For the reason that said opinions, findings and orders on their face show the contract between plaintiff and the Cities Service Gas Company to be such a contract as would have been entered into by parties unaffiliated dealing at arm's length and in the general and open market subject to the usual safeguards of bargaining and competition.

(d) For the reason that said Commission in dealing with the item of interest during construction, as appears in Exhibit "C," pages 78 and 79, found that 6 per cent was a proper rate to use for this item notwithstanding the fact that it is common knowledge of which the Court may take judicial notice that money could not be procured at the time of said hearing at such rate and notwithstanding the fact that the Commission found 7 per cent to be a proper rate of return for the Cities Service Gas Company after the completion of its plant and after the same was placed in operation, said Commission by adopting said 6 per cent having thereby eliminated from the rate base of the Cities Service Gas Company approximately one million dollars. . .

(e) For the reason that in its consideration of the item of going value as appears in Exhibit "C," pages 85 to 88, the Commission unlawfully, unreasonably, arbitrarily and capriciously allowed only the sum of $2,000,000.00 on its own valuation of $73,148,510.00 and ignored all the evi- [fol. 22] dence in the case on the subject, such evidence consisting of the testimony of F. C. Hamilton, engineer for plaintiff, that a proper allowance would be $8,898,532.00, and the testimony of its own witness, E. B. Black, that such value was $3,820,000.00, and ignored the uniform practice of courts and commissions to allow for such item approximately 10 per cent of the rate base, by which arbitrary and unreasonable action said Commission reduced the proper rate base of said Cities Service Gas Company over six million dollars.

(f) For the reason that said Commission in its consideration of the item of gas leases and reserves of said Cities Service Gas Company after finding that the present fair market value of such reserves was $6,279,237.00 and the present book value $6,573,489.70, as appears in Exhibit "C" at pages 99 and 100, unreasonably and arbitrarily found that most of said reserves were not used and useful

and allowed for said item only the sum of $2,874,390.00, thereby eliminating from the rate base of the Cities Service Gas Company the sum of $3,404,847.00, which on its own finding of present market value should have been included; and said Commission on rehearing wrongfully refused to permit plaintiff to show that the reserves allowed by said Commission were inadequate and would result in absolute failure of service as is shown by Exhibit "G" hereto attached. By all of which unreasonable, arbitrary and unwarranted conduct said Commission undertook, without one word of evidence from any witness in support of its finding as to what would constitute proper reserves for said Cities Service Gas Company, to substitute its own judgment and to usurp the duties of the officers of said company upon whom the responsibility for service rests.

[fol. 23] (g) For the reason that said Commission eliminated from the replacement reserves of the Cities Service Gas Company all lease rentals and development expense on leases which it wrongfully found to be not used and useful, amounting to the sum of $532,530.77, as appears from said order, Exhibit "C," at page 112, and also eliminated the reserve which must be accrued for amortizing the cost of said leases, amounting to $314,981.68, as appears from said order, Exhibit "C," page 112, or a total of $847,512.45.

(h) For the reason that said Commission, in determining the rate base of the Cities Service Gas Company, depreciated overheads, thereby eliminating from said rate base the sum of $1,011,392.00, without making any allowance in replacement reserves to compensate for such depreciation, which reserve should have been included in the amount of $30,443.00 annually, as appears by the opinion of said Commission, Exhibit "C," at page 111, or said overheads should not have been depreciated and said rate base should have been accordingly increased.

(i) For the reason that it is apparent on the face of said opinions, findings and orders that if said Commission had made proper allowances in the rate base of the Cities Service Gas Company for interest during construction, going value and leases and gas reserves, and had made reasonable allowances for replacement reserves, the rate base of said Cities Service Gas Company would be so in-

creased and its earnings after replacement reserves so decreased on the Commission's own findings that the present earnings of said company after reserves and applicable for return would amount to less than 6¼ per cent on such rate base.

(j) For the reason that said Cities Service Gas Com-
[fol. 24] pany is engaged in interstate commerce the right to control which is vested by the Constitution of the United States exclusively in Congress, and said Commission is without jurisdiction to fix a rate for said company or to proceed in the manner attempted in said proceedings so instituted by it or to make the orders herein set out.

(k) For the reason that the value of the property of the Cities Service Gas Company used and useful in carrying on its said business on August 31st, 1932, and at all times since that date, was and is not less than $105,857,402.00, and the finding by said Commission in said opinion and orders of August 31st, 1932, that said value was only the sum of $73,148,510.00 is unreasonable, unjust and contrary to all the evidence introduced before said Commission.

(l) For the reason that if the price of 30 cents for gas sold for domestic purposes at the city gate by the Cities Service Gas Company had been in effect during the year ending June 30th, 1932, and if said rate of 30 cents per M. C. F. is applied to the actual business transacted by said Cities Service Gas Company for said period, its gross earnings would have been reduced in the sum of $1,926,145.07 and its net earnings before replacement reserves would have been $5,935,371.78, which is a return of only 5.4 per cent on said Commission's own rate base as found in said opinion and orders of $73,148,510.00, which rate base is entirely unreasonable, unjust and inadequate as hereinbefore alleged after deducting the Commission's own unreasonable, unjust and inadequate allowance for replacement reserves, and if said rate had been so applied during said period the earnings of the Cities Service Gas Company would have amounted to only 5.6 per cent on the present fair value of its property of $105,857,402.00 for
[fol. 25] all the purposes of replacement reserves, depreciation, amortization, depletion and return.

(m) For the reason that in its consideration of the reasonableness of said contract between plaintiff and Cities Service Gas Company for plaintiff's supply of gas at the city gate it was the duty of said Commission, in the absence of any jurisdiction, power or authority over the interstate business of said company, to consider its operations, business and experience as the same actually existed and were being carried on by said company, without undertaking or attempting to determine the reasonableness or usefulness of its gas reserves or any other item of its property and without undertaking or attempting to determine the reasonableness of its operating expenses, or any item thereof, the jurisdiction of said Commission being limited to the determination of the reasonableness of such contract under existing operating conditions of the Cities Service Gas Company and said Commission being without jurisdiction, power or authority to regulate said company as attempted in said opinions, findings and orders.

(n) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(o) For the reason that the finding of said Commission that the contract between plaintiff and Cities Service Gas Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said [fol. 26] Commission in said proceedings and is entirely without support in the evidence.

(p) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A," herein and all subsequent proceedings of said Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to

ascertain the reasonableness of a rate or charge to be made by a public utility.

26

Contract with Henry L. Doherty & Company

Plaintiff further alleges that said opinion and orders of said Commission entered August 31st, 1932, and each and all of them, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which plaintiff pays to said Henry L. Doherty & Company 1¾ per cent of its gross revenues, are unreasonable, unjust, unlawful and void for the following reasons:

(a) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(b) For the reason that said Commission in said investigation so held by it did not have before it any evidence whatever as to the value of plaintiff's property used and useful in rendering the service in which it is engaged, [fol. 27] its operating experience or the reasonableness of its existing rates, and unlawfully, unreasonably and unjustly refused to permit plaintiff to introduce any such evidence and was therefore not in a position to determine whether or not the disallowance of said item of operating expense world affect the rates then being charged by plaintiff or warrant a decrease in rates to consumers.

(c) For the reason that said Commission was without jurisdiction, power or authority to disallow said item of plaintiff's operating expense in the absence of an express finding that existing rates were unreasonable by reason of the inclusion of said item in plaintiff's operating expenses and the substitution of a new rate in lieu of the old rate so found to be unreasonable.

(d) For the reason that plaintiff offered to show to said Commission in said original proceeding and on rehearing,

as shown by Exhibit "F" hereto attached, that under existing rates it was earning only 7.2 per cent on the present fair value of its property, and the disallowance of said item in plaintiff's operating expenses could not possibly affect the reasonableness of its existing rates or give jurisdiction to the Commission to reduce the same on account of the disallowance of said item.

(e) For the reason that said Commission by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment has unlawfully and unreasonably undertaken the management of plaintiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

(f) For the reason that the finding of said Commis-
[fol. 28] sion that the contract between plaintiff and Henry L. Doherty & Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceeding and is entirely without support in the evidence, while in truth and fact services of great value were and are being rendered by said Henry L. Doherty & Company, to-wit, the amount charged.

27

Reduction in Rates

Plaintiff further alleges that said orders of said Commission herein recited and set out and each and all of them, in so far as they purport to change, alter and reduce the rates of this plaintiff to be charged by it to its consumers, are unreasonable, unlawful, arbitrary and void for the following reasons:

(a) For the reason that said orders, and each of them, and particularly said order, Exhibit "M," directing this plaintiff to reduce its rates to consumers as of September 1st, 1932, is in direct violation of Section 66-115, Re-

vised Statutes of Kansas of 1923, which statute expressly provides that all orders of said Commission "shall be in force and effect on and after 30 days from the making thereof."

(b) For the reason that this plaintiff was unlawfully, unreasonably and arbitrarily denied an opporunity to present to said Commission evidence as to the value of its property, its earnings and its general operating experience un- [fol. 29] der the rates now being charged by it, and to show to said Commission that for the year ending June 30th, 1932, its earnings under existing rates produced a return of only 7.2 per cent on the present fair value of its property, said 7.2 per cent being the earnings of said company for said period for both depreciation and return, and to show that any reduction in existing rates would be unreasonable, unjust and would result in the confiscation of its property, all of which this plaintiff offered and demanded the opportunity to show as is set out in Exhibit "F," hereto attached.

(c) For the reason that the Commission did not investigate the reasonableness of the existing rates of this plaintiff, did not have before it any evidence as to the value of plaintiff's property or any evidence as to its operating experience, or make any investigation whatever as to any such matters, or any other matters concerning the reasonableness of its present rates, as required by Sections 66-110 and 66-113, Revised Statutes of Kansas of 1923, and other statutes of the State of Kansas, such investigation being required before such Commission has any jurisdiction, power or authority whatever over the rates of this plaintiff and its jurisdiction to act in the premises being entirely dependent upon a previous investigation of relevent facts.

(d) For the reason that said Commission did not find the existing rates of this plaintiff to be unjust, unreasonable, unjustly discriminatory, or unduly preferential, or otherwise in violation of the statutes of the State of Kansas, as is expressly required by Section 66-110 and Section 66-113, Revised Statutes of Kansas of 1923, and other sections of said Act, and had before it no evidence upon which any such finding could have been made, and [fol. 30] for the reason that in the absence of such finding

said Commission is without any jurisdiction, power or authority to change, alter or amend in any manner the existing rates of this plaintiff.

(e) For the reason that said Commission did not fix and order substituted for the present rates of this plaintiff any other or different rate as is required by Section 66-110, Revised Statutes of 1923, and other laws of the State of Kansas, but merely undertook to order this plaintiff to pass on to its consumers a theoretical saving in its expenses in an amount undetermined and impossible of determination and which amount varies in accordance with the variation in business transacted by this plaintiff on each and every day of its operation, such order being in said respect so ambiguous, indefinite and meaningless as to be impossible of performance.

(f) For the reason that the existing rate of plaintiff established by order of said Commission consists of a charge of .145 per 100 cu. ft. for 1st 1,000 cu. ft. per month, .095 per 100 cu. ft. for next 2,500 cu. ft. per month, .05 per 100 cu. ft. for next 146,500 cu. ft. per month; .023 per 100 cu. ft. for balance of monthly delivery that the form of said rate is such that even a determined and definite reduction to be passed on to consumers could not be applied thereto without a direction as to which step or block in said rate should be charged and how said reduction should be spread over the monthly consumption of any customer, said order being in said respect so indefinite and ambiguous as to be impossible of performance.

(g) For the reason that said Commission without investigation, without finding the unreasonableness of existing rates and without affording plaintiff its day in court, [fol. 31], or an opportunty to be heard, undertook to order a reduction in existing rates immediately effective and to then at a later time hold such proceeding as is required by law in the first instance for the purpose of determining whether its previous order reducing rates should have been made and entered, thereby requiring plaintiff to suffer the confiscation of its property during the entire rate making period.

(h) For the reason that plaintiff has been notified by the Cities Service Gas Company that it will not recognize the order of said Commission and will not sell and deliver gas

to plaintiff for domestic purposes at a less price than 40 cents per M. C. F. at the city gate and if plaintiff should reduce its rates to consumers at this time and as required by said order, it would be placed in the position of guaranteeing the validity of said order and in the event the same should be held to be unlawful, unreasonable or set aside for any other reason, this plaintiff would be irreparably injured and damaged for the reason that it could not recoup from its consumers the loss it would sustain in the event said Cities Service Gas Company should compel it to pay 40 cents per M. C. F. for the gas so sold and delivered to it.

(i) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expense.

(j) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A", herein and all subsequent proceedings of said [fol. 32] Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to ascertain the reasonableness of a rate or charge to be made by a public utility.

(k) For the reason that said Commission, by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment, has unlawfully and unreasonably undertaken the management of plantiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

28

Plaintiff further alleges that said defendant Commission was without jurisdiction, power or authority to proceed against utilities generally in one joint proceeding and to compel plaintiff to have joined with it others with which it had nothing in common; that the entire proceeding had before said Commission was beyond its jurisdiction; that

plaintiff was unlawfully and wrongfully compelled to appear before said Commission and that the objections of the plaintiff as set out in Exhibit "B" should have been sustained.

29

Plaintiff further alleges that for all of the reasons hereinbefore set out said proceedings before said Commission and all opinions, findings and orders made by it therein are unreasonable, unjust, unlawful and void in that they deprive [fol. 33] plaintiff of its property without due process of law; deny it the equal protection of the law; impair the obligation of its contracts; undertake to legislate with respect to interstate commerce and usurp the business management of the plaintiff company, all in violation of the Constitution and laws of the United States and of the State of Kansas, and particularly Clause 3 of Section 8 of Article 1, the first subdivision of Section 10 of Article 1 of the Constitution of the United States and the Fourteenth Amendment thereto.

30

That plaintiff cannot procure gas for the requirements of its business from the Cities Service Gas Company for less than 40 cents per M. C. F. and if it is, by said orders of said Commission, compelled to pay said sum for purchased gas and base its rates to consumers on a price of 30 cents per M. C. F., it cannot make a fair or reasonable return on the fair value of its property, and its property will be confiscated, all of which is in violation of and repugnant to the Constitution and Laws of the United States as alleged in the next preceding paragraph hereof.

31

Plaintiff alleges that it is the intention and purpose of said defendants to attempt to intimidate plaintiff into the acceptance of said orders of August 31st, 1932, by instituting proceedings against plaintiff and its correspondents in said proceeding before the Commission for the appointment of receivers for their several properties, and under date of September 16th, 1932, in pursuance of said intention [fol. 34] and purpose and at the instigation of said defendant, The Public Service Commission, the Governor of the State of Kansas ordered the defendant Roland Boynton,

Attorney General of said state, to institute court proceedings seeking dissolution of said several companies and the appointment of receivers for them and said Attorney General has stated that he will obey the directions of said Governor; that the effect of the filing of such proceedings will be to adversely affect plaintiff's public relations, destroy confidence of its stockholders, affect its financial standing and otherwise embarrass it, and will affect its ability to render service to its consumers; that the purpose of said proceedings is to intimidate and coerce plaintiff into the acceptance of said orders and also to take the conduct of plaintiff's business out of the hands of its officers and prevent it from contesting said orders in this or any other court; that plaintiff has never been requested or directed by said defendants or any other officer of the State of Kansas to transact its business in any manner different from that in which it is now being conducted and plaintiff stands ready and willing at any time to comply with the lawful orders or directions of any court or officer respecting any of its corporate practices; that without regard to plaintiff's ability to defend itself in any such proceedings if brought, the filing of such charges and consequent publicity will cause it irreparable damage and injury.

32

Plaintiff further alleges that in its supplemental application for a rehearing, Exhibit "O" herein, it called to the attention of said defendant Commission the fact that a certain order had been issued by the regulatory body of the [fol. 35] State of Texas having jurisdiction in the premises restricting the amount of gas which said Cities Service Gas Company could take from wells on its gas reserves to 4 per cent of the potential capacity of such wells, which application was by said Commission denied as shown by its order of September 12th, 1932, as being without merit for the reason as plaintiff is informed and believes, that said defendant Commission after communication with said regulatory body of the State of Texas was informed that said restriction of 4 per cent did not apply to the requirements of pipe lines for domestic and industrial use; that plaintiff is informed that on September 16th, 1932, said regulatory body of the State of Texas amended its original order so as to eliminate from its restriction of 4 per cent gas used for

domestic and industrial purposes, leaving said restriction as an absolute and unqualified limitation on the takes from all wells in the gas reserves of the Cities Service Gas Company, thereby making the gas reserves allowed by said Commission as herein before set out entirely inadequate, insufficient and unreasonable.

33

Plaintiff is without adequate remedy at law in the premises herein before set forth and will suffer irreparable injury unless accorded the injunctive relief herein prayed for; that the penalties provided for the infraction of orders of said Commission are so enormous, cruel and unusual as to intimidate plantiff and to force it to abandon any rights it may have to act independently thereof; that plaintiff will be unable to make collection from its consumers for gas sold and delivered to them if it attempts to act contrary to said orders and in the absence of the relief herein prayed [fol. 36] for plaintiff is unable to protect itself against the same.

Wherefore, since plaintiff is without adequate remedy save in a court of equity, it prays:

(A) That the said defendants, and each of them and all persons acting through or under them, be permanently restrained and enjoined from the enforcement of said orders of August 31st, 1932, or from interfering with the existing rates of plaintiff or its contracts with Henry L. Doherty & Company and Cities Service Gas Company by reason of said orders, or either of them, and from commencing, instituting or prosecuting in this or any other court or tribunal any suit or proceeding to litigate any of the matters herein complained of or the purpose of which is to compel or intimidate plaintiff to accept said orders or deprive it of its right to prosecute this or any other proceeding to contest the validity of said orders.

(B) That this cause be set for hearing on application for temporary injunction at an early date and that upon said hearing the court issue its temporary injunction enjoining said defendants, and each of them, from the enforcement of said orders and that pending said hearing the court enter its restraining order with like effect.

(C) That the plaintiff have such other and further relief as may be just and equitable.

(D) That there be issued out of this Court a writ of subpœna to be served upon the defendants, The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, thereby commanding them, and each of them, at a certain time and under a certain penalty therein to be limited, personally to appear before this Honorable Court and then and there full, true, direct [fol. 37] and perfect answer make to all and singular in the premises and further to stand to perform and abide such further order, direction and decree therein as shall seem agreeable to equity and good conscience; and your plaintiff will ever pray.

Robt. D. Garver, Robert Stone, Attorneys for Plaintiff.

*Duly sworn to by Robert D. Garver. Jurat omitted in printing.*

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[fol. 38] EXHIBIT "A" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Co., Wichita;
" B. Hutchinson Gas Co., Hutchinson;
" C. Newton Gas Co., Newton;
" D. Pittsburg Gas Co., Pittsburg;
" E. Capital Gas & Electric Co., Topeka;
" F. Wyandotte Gas Co., Kansas City, Kansas;
" G. Arkansas Valley Gas Co., Arkansas City;
" H. Girard Gas Co., Girard;
" I. Union Public Service Co., 45 Towns;
" J. Western Dist. Co., 27 Towns;

" K. Winfield Natural Gas Co., Winfield;
" L. Tri-City Gas Co. a/c Gas Service Co., Kansas City, Mo.;
" M. Gas Service Co., Kansas City, Mo.;
" N. American Pipe Line Co., Bartlesville, Okla.,

*Respondents.*

Order for Investigation

Now on this second day of July, 1931, it appears to the Public Service Commission for the State of Kansas, that the reasonableness of all contracts, and charges made by holding companies to subsidiary companies of the Cities Service Company (respondents above named) operating within the State of Kansas, should be inquired into for the [fol. 39] purpose of determining the reasonableness of such contracts and the reasonableness of the charges made for services and commodities furnished.

It further appears to the Public Service Commission that the holding companies of the said subsidiary companies occupy a special position with particular advantages in relation to the sale of gas and contracts for service and commodities furnished; and that the holding companies through stock ownership dominate and control the management of the said subsidiary companies.

The Commission therefore finds that the contracts made and charges for services rendered and commodities furnished to said subsidiary distributing companies by the holding companies and Henry L. Doherty & Company should be inquired into to determine their reasonableness and to find what amount should be allocated in this respect to the operating expense of the subsidiary companies.

It is therefore by the Commission ordered: That an investigation be set for hearing on the 18th day of August, 1931, at 10 o'clock a. m., at the office of the Commission in Topeka, Kansas, to inquire into the reasonableness of contracts made with, and the services rendered to, the subsidiary companies of the Cities Service Company by their various holding companies.

It is further by the Commission ordered: That each of the above-named respondents appear on the above-mentioned date to give to the Commission such information as they may desire on their own behalf, and as may be required by the Commission, in behalf of said investigation, and to show

cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the [fol. 40] distributing companies, and adjustment made in this respect as to charges made to the consumers.

By the Commission it is so ordered.

J. W. Greenleaf, Thurman Hill, Chas. W. Campbell, Commissioners. Attest: C. H. Benson, Secretary.

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EXHIBIT "B" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges made by Holding Companies to Subsidiary Companies of the Cities Service Company

Entry of Appearance and Objections of The Wichita Gas Company

Comes now The Wichita Gas Company, a Kansas corporation, in compliance with the order of this Commission herein dated July 2nd, 1931, and hereby enters its appearance for the purpose of furnishing to this Commission all information which it has or is able to procure in regard to the contracts recited in said order.

Said respondent hereby expressly limits its appearance and appears specially for said purposes and said purposes only hereby expressly objecting to any consideration by this Commission in this proceeding of the reasonableness [fol. 41] or unreasonableness of its existing rates or any attempt to change the same by reason of any findings which this Commission may make in respect to said contracts from the evidence introduced herein and expressly denying the jurisdiction of the Commission to consider in this proceeding any issue as to the value of respondent's property, the adequacy or inadequacy of its earnings or the reasonableness or unreasonableness of its rates for the following reasons:

1. That the Commission has no juridiction, power or authority, under the laws of the State of Kansas, to proceed against utilities generally in one joint proceeding and to compel one utility to have joined with it others with which it has nothing in common.

2. That this respondent owns and operates a public utility only in the City of Topeka, Kansas, and its immediate environs, and its rates are, by law, required to be determined with respect to the value of its property used and useful in rendering its public service and without regard to the value of the properties of the other utilities joined herein.

3. That the other parties respondent to this proceeding are improperly joined with the respondent and are not necessary or proper parties as far as any proceeding against this respondent is concerned which involves a consideration of its rates.

4. That each public utility and each respondent herein as to each property which it operates is entitled, under the law, to a full, complete and separate hearing as to each such city or community and the rates as to each such city or community must be considered by this Commission separate and apart and without regard to the property or rates of any other utility.

5. That it will be impossible, in this proceeding, for any [fol. 42] utility to make a record covering proceedings affecting it without including therein proceedings concerning other utilities and impossible for such utility to avail itself of the right of appeal or review provided by law.

6. That each utility respondent herein is deprived of the right to conduct its cause according to its independent judgment and in a legal and orderly manner and to avail itself of the rights granted and guaranteed by the Constitution and Laws of the United States and of the State of Kansas.

7. That the existing rates of this respondent are inadequate, unremunerative and confiscatory in that they do not enable respondent to earn a fair return for all purposes on the fair value of its property and that no change in such rates can lawfully be made without affording respond-

ent an opportunity to present all pertinent facts relating to the value of its property and its financial experience, which opportunity cannot be adequately afforded in this proceeding wherein respondent is joined with utilities operating in some one hundred and eighty towns and communities, the rates for each of which must be determined by considerations entirely independent of every other property.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

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[fol. 43] EXHIBIT "D" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Application of the Wichita Gas Company for Rehearing

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, applies for a rehearing in respect to all matters found and ordered and purported to have been determined herein by this Commission for the reason that its decision, findings and order, severally and collectively, are unlawful, unjust and unreasonable in the following respects and for the following reasons:

1

For the reason that in its investigation of the contract between the respondents and the Cities Service Gas Company for the supply of gas at the city gates of the respective cities served by respondents, the Commission has approached all questions involved the same as if it had power and jurisdiction under the law to fix the rates and commodity charges of the Cities Service Gas Company, a

corporation engaged in interstate commerce, and has, in effect, undertaken to fix the rates and commodity charges [fol. 44] of said interstate company in relation to its interstate business and has undertaken to and has fixed the rates and commodity charges for said company, the authority to do which is, by the Constitution of the United States, vested exclusively in the Congress of the United States, and by its decision and order said Commission has usurped the exclusive power of Congress and has acted wholly without legal authority, power or jurisdiction.

2

For the reason that the gas purchased by said respondents respectively at their respective city gates is natural gas transported by the Cities Service Gas Company in interstate commerce, national in its character, and said Cities Service Gas Company is lawfully entitled to sell said gas to the several respondents herein and to other like purchasers in the several states through which its transportation system passes without interference by the Commissions of the several state in which such interstate transaction is carried on and said decision, opinion, findings and order unlawfully deprive said Cities Service Gas Company of the fruits of said interstate transportation and unlawfully deny to it the free right to sell from its said transportation system its product so transported and unlawfully deprive it of the rights guaranteed to it by Clause 3 of Section 8 of Article 1 of the Constitution of the United States.

3

For that reason that said decision, opinion, findings and order, severally and collectively, and every part thereof, are in violation of Clause 3 of Section 8 of Article 1 of the [fol. 45] Constitution of the United States in that they seek to impose an unreasonable regulation and an undue burden on intertsate commerce, national in character, that can be imposed only by the Congress of the United States.

4

For the reason that said decision, opinion, findings and order are in violation of the first subdivision of Section 10 of Article 1 of the Constitution of the United States

in that they, and each of them, impair the obligation of the contracts of the Cities Service Gas Company and the contracts of this and the other respondents.

5

For the reason that said decision, opinion, findings and order, and every part thereof, are in violation of the Fourteenth Amendment to the Constitution of the United States in that they deprive Cities Service Gas Company and the respondents, and each of them, of their property without due process of law, destroy their freedom of contract and deny to them the equal protection of the law.

6

For the reason that the rate found by said Commission to be a reasonable price to be paid for gas at the gates of the cities supplied by respondents, respectively, is a rate that would not produce a reasonable return on the fair value of the property of the Cities Service Gas Company used and useful in such service; would result in the confiscation of its property and deprive it of its property without due process of law, all in violation of the Constitu-
[fol. 46] tion of the United States and the laws and Constitution of the State of Kansas.

7

For the reason that the Cities Service Gas Company, in the sale of its product so transported in interstate commerce, national in character, is limited to the market connected with its transportation system, as now located, and that by its order to the several respondents herein it, in effect, deprives said Cities Service Gas Company of all market for its gas at rates other than those attempted to be established by said Commission in said decision, opinion, findings and order and deprives it of the right to carry on its business and deprives it of its property without due process of law, all in violation of the Constitution of the United States.

8

For the reason that said decision, opinion, findings and order in so far as they relate to the contract between this

respondent and Henry L. Doherty & Company and under which this respondent pays to Henry L. Doherty & Company 1¾ per cent of its gross revenue in compensation for the services rendered by said Henry L. Doherty & Company, impair the obligation of such contract; deny to respondent and to said Henry L. Doherty & Company the free right of contract; undertake the business management of the respondent company; usurp the duties of the officers and directors of said companies, respectively, and substitute the opinion and conclusion of said Commission for the business judgment of the officers and directors of said companies as to matters of purely business policy, all in viola- [fol. 47] tion of the Constitution of the United States and the Constitution and laws of the State of Kansas.

9

For the reason that said decision, opinion, findings and order, in so far as they relate to the contract between this respondent and Cities Service Gas Company and under which this respondent purchases its supply of gas for distribution to its consumers, impair the obligation of such contract; deny to respondent and to said Cities Service Gas Company the free right of contract; undertake the business management of the respondent company and the Cities Service Gas Company; usurp the duties of the officers and directors of said companies, respectively, and substitute the opinion and conclusions of said Commission for the business judgment of the officers and directors of said companies as to matters of purely business policy, all in violation of the Constitution of the United States and the Constitution and laws of the State of Kansas.

10

For the reason that said respondent has been informed and notified by said Cities Service Gas Company that it will not supply it with gas at the rate prescribed by said Commission in its said decision, opinion, findings and order; that respondent is without any other supply of gas with which to perform the public service in which it is engaged and that if said decision, opinion, findings and order become effective its ability to render service will be destroyed and it will have to discontinue service entirely.

[fol. 48] 11

For the reason that said decision, opinion, findings and order undertake to compel respondents, and each of them, as of August 1st, 1932, to pass on to their respective consumers a reduction of ten cents per 1,000 cubic feet, without an opportunity to be heard in the manner provided by the statutes of the State of Kansas or otherwise as to whether or not their rates would be reasonable and lawful in the event such reduction should be made as ordered.

12

For the reason that this respondent is now operating under insufficient and confiscatory rates and even if a reduction in its expenses could be effected, as provided in said decision, opinion, findings and order, the rates of respondent would still not be unreasonably high and would be less than it is entitled to lawfully charge.

13

For the reason that in the course of this proceeding said Commission refused to permit this respondent to show the present fair value of its property used and useful in rendering the service in which it is engaged and its financial experience under the rates now in effect, evidence in respect to which was offered by respondent in an effort to show that even if a reduction in the city gate rate should be ordered by the Commission its existing rates would not be affected, said Commission in that connection having informed respondent in open court that no such reduction was contemplated or would be attempted in any order which might be made as the result of said proceedings, by [fol. 49] which conduct of the Commission respondent was misled, misinformed and dec-ived as to the issue before said Commission, was deprived of a lawful hearing and was denied the opportunity of presenting their evidence.

14

For the reason that said decision, opinion, findings and order, in so far as they purport to order a reduction in the

rates charged by this respondent, are not supported by any evidence whatever as to the value of the property of this respondent, its financial experience or any other fact or evidence which would enable the commission to determine reasonable rates for it to put into effect.

15

For the reason that said Commission is entirely without jurisdiction to change, alter, or in any manner affect the rates being charged by respondent without a finding based on substantial evidence that the present rates of respondent are unreasonable or unlawful and no such finding has been made in this proceeding.

16

For the reason that said decision, opinion, findings and order undertake to put in effect reduced rates as of August 1st, 1932, prior to the time this application for rehearing, made mandatory under the statutes of Kansas and a condition precedent to any action in the courts attacking said decision, opinion, findings and order, can be submitted or passed upon by said Commission, whereby respondent is deprived of remedies afforded by the statutes of the State of Kansas for its protection.

[fol. 50] 17

For the reason that said decision, opinion, findings and order, and each of them and all parts thereof, are unsupported by the evidence and are contrary to the evidence.

18

For the reason that said decision, opinion, findings and order, and each of them and all parts thereof, are unreasonable, unjust and contrary to law.

19

For the reason that said decision, opinion, findings and order result in an unreasonable, unjust and unlawful discrimination in that they permit companies not affiliated with the Cities Service Gas Company to purchase their

supply of gas from the Cities Service Gas Company at a rate different from any permitted to be paid by respondent.

20

For the reason that in its said decision, opinion, findings and order the Commission erroneously attempted to average values and earnings over certain periods of time and by its failure to include certain items of property in use at a given time computed earnings on a much lower rate base than actually existed, thereby arriving at an entirely erroneous conclusion; that at the present time a full year's financial experience can be had on all property comprising the rate base of the Cities Service Gas Company and respondent asks an opportunity to make such showing, thereby eliminating all necessity for speculation and conjecture.

[fol. 51]

21

For the reason that there has been a change in conditions since the periods which the Commission considered in the hearings had herein so marked and exceptional as to constitute "the outstanding contemporary fact, dominating thought and action throughout the country" and of which the Commission must take judicial notice (284 U. S. 248) and such changed conditions have made the past financial experience of the Cities Service Gas Company, as shown by the evidence herein, no further applicable, competent or relevant.

22

For the reason that the valuation of the property of the Cities Service Gas Company used in its purported rate base is not the value of said property as of the date of said hearing, or the date agreed upon.

23

For the reason that the earnings of said Cities Service Gas Company found by said Commission to have been earned on the rate base found by it are not the earnings being made at the time of said hearings, or the date agreed upon.

24

For the reason that the earnings of the Cities Service Gas Company, at the time of said hearings, were not in excess of a reasonable return on the then fair value of its property.

[fol. 52]

25

For the reason that the Commission unlawfully and unreasonably usurped the prerogatives, duties and authority of the officers and directors of Cities Service Gas Company, upon whom the responsibility for service rests, and arbitrarily and unlawfully refused to include in the rate base of said company and in the value of its property leases of the value of many millions of dollars for the reason that said leases were not, in the opinion of said Commission, presently used or useful, such action of the Commission being wholly unsupported by any evidence and being entirely arbitrary.

26

For the reason that this respondent, in entering into its contract with the Cities Service Gas Company for its supply of gas, relied upon the gas reserves of said Cities Service Gas Company as then and now owned and controlled by it and contracted with respect to such reserves which, in the opinion of this respondent, were necessary to secure an adequate and lasting supply of gas and guarantee service to its consumers.

27

For the reason that said Commission eliminated from the operating expenses of Cities Service Gas Company rentals on leases which, in the business judgment of the officers of said company and of this respondent, are necessary to constitute adequate, proper and necessary gas reserves for its system, thereby unreasonably and unlawfully substituting their opinions and conclusions for the business judgment of the officers and directors of said [fol. 53] companies, such opinions and conclusions being wholly without support in the evidence.

28

For the reason that said Commission eliminated from the operating expenses of Cities Service Gas Company all

sums paid by it to Henry L. Doherty & Company as representing 1¾ per cent of its gross receipts from gas sold by it to unaffiliated distributing companies and other purchasers, said Commission having no jurisdiction, authority or power whatever over such contracts, its sole jurisdiction being dependent upon affiliation or the absence of arm's length dealing and also for the reason that said contract as between this respondent and Henry L. Doherty & Company was disapproved by the Commission on the basis that the services rendered by Henry L. Doherty & Company were a duplication of services rendered by The Gas Service Company whereas no services are rendered by The Gas Service Company to the Cities Service Gas Company or to unaffiliated distribution companies or to any other purchasers of gas from the Cities Service Gas Company and no such duplication could exist as to such contracts.

29

For the reason that the value found by said Commission of the property of the Cities Service Gas Company entirely ignores all testimony and evidence introduced before said Commission, including the state's own witnesses and is contrary to all evidence in the case.

[fol. 54] 30

For the reason that in its allowance of replacement reserves the Commission arbitrarily disregarded the only evidence in the case, which was the testimony of witnesses for respondents as to proper reserves for the Cities Service Gas Company, determined by the actual past experience of the company and the business judgment of its officers and directors to be proper, and in lieu thereof and without any support whatever in the evidence allowed an amount for replacement reserves based on the percentages which the reserves testified to by respondents' witnesses happen to bear to the value of the property of Cities Service Gas Company as claimed by it and as testified to by respondents' witnesses and applied such percentages so obtained to the erroneous value found by it for a part only of the property of the Cities Service Gas Company, which value is contrary to all evidence before the Commission, and the reserves so determined and allowed are entirely inadequate for the purposes intended.

31

For the reason that in a proceeding involving only the reasonableness of a contract for purchased gas the decision, opinion, findings and order of the Commission are un-*un*reasonable, unjust and unlawful in limiting said Cities Service Gas Company to a return of seven per cent after replacement reserves, such allowance being contrary to all evidence in the case and entirely inadequate under present economic conditions, a reasonable return as shown by the evidence being eight per cent and there being no evidence to the contrary.

[fol. 55]

32

For the reason that the decision, opinion, findings and order of the Commission, in so far as they purport to determine whether rates of the several respondents should be reduced and order a reduction thereof, are unreasonable, unlawful and void as not properly within the issues framed by the original order initiating this investigation and are contrary to the express statement of the issues by the Commission and its attorneys in open court (R. 8, 2859 to 2867, inc.) to the effect that if a reduction in the city gate rate should be ordered an opportunity would be given all distributing companies, respondents herein, including this respondent, to separately show the value of their property and their financial experience under existing rates before such rates would be changed.

33

For the reason that the Commission is without power, authority or jurisdiction to order a change in the rates of this respondent without the statutory notice that such change in rates is in issue and without affording the respondent an opportunity to present evidence showing the value of its property and its experience under existing rates, and for the reason that said order is made effective August 1st, 1932, contrary to law.

34

For the reason that the order of the Commission directing a reduction in the rates of this respondent as of August 1st, 1932, with the further order that respond-

ent appear on September 1st, 1932, to show cause why the reduction ordered should not be permanently con-
[fol. 56] tinued in effect, is unreasonable, unlawful, beyond the power and jurisdiction of the Commission and void for the reason that it would compel the respondent to suffer confiscation during the rate making period and for the reason that said order to show cause on September 1st is, in effect, an admission that the rate reductions ordered were made without a consideration of the necessary facts by the Commission and without an opportunity having been afforded this respondent to be heard on the issue as to whether or not its rates should be reduced.

35

For the reason that the order to show cause on September 1st, 1932, as to why a rate reduction should not be made permanent requires the respondents to be prepared on complete rate cases, including detailed valuations and financial studies and exhibits for ten companies doing business in almost one hundred separate cities and communities and involving property of the value of approximately $15,000,000.00, the preparation of which cases in the proper manner would require at least a year's time and the orderly and proper hearings of which matters would require months, all of which is physically impossible of performance on September 1st, 1932, and the result of said order would be that said reductions in rates so made without any issue being raised, evidence introduced or opportunity afforded for a hearing would be in effect for perhaps several years during which time respondents, and each of them, would be unlawfully deprived of a fair earning on the fair value of their properties respectively and their properties would be confiscated, taken without due process of law and they, and each of them, would be denied [fol. 57] the equal protection of the law, all in violation of the laws and Constitution of the State of Kansas and the Constitution of the United States.

36

For the reason that if the parts of said decision, opinion, findings and order directed to these respondents and calling for and ordering a reduction in their respective rates should be eliminated from said order there would remain

only a determination of the moot question as to the value of the property of the Cities Service Gas Company and an unlawful determination of what its rates should be at the several city gates, the right to determine which rests exclusively in the Congress of the United States and is wholly without the jurisdiction of this Commission.

37

For the reason that the Commission in its decision, opinion, findings and order did not value the property of the Cities Service Gas Company as of the time of said proceedings but erroneously attempted to arrive at an average value which does not represent the value of the property of said company at any certain time.

38

For the reason that the Commission in its said decision, opinion, findings and order did not ascertain the earnings of the Cities Service Gas Company as of the time of said proceedings or as of any definite time but erroneously undertook to average the same over a period of years, thereby arriving at an erroneous conclusion as to earnings which has no proper relation to the value of the property of the Cities Service Gas Company.

[fol. 58] 39.

For the reason that figures are now available showing the financial experience of the Cities Service Gas Company for the year ending June 30th, 1932, which figures were not available at the time of the several hearings herein or at the time said hearings were concluded, such presently available figures and experience show that the net earnings of the Cities Service Gas Company for all purposes and before replacement reserves were $7,865,110.82 for the year ending June 30th, 1932; that in its said decision, opinion, findings and order the Commission found a rate base for the Cities Service Gas Company as of September 1st, 1931, of $73,073,713.00 and further found that said company was entitled to earn thereon 7 per cent for return and approximately 3 per cent for replacement reserves, or a total of approximately ten per cent, or $7,087,751.00; that if the rate of 29½ cents per thou-

sand cubic feet, found by the Commission to be a proper rate, had been in effect during the year ending June 30th, 1932, the earnings of Cities Service Gas Company would have been $5,777,110.00 or $1,310,641.00 less than a fair and reasonable return even if computed on the Commission's own rate base and on the Commission's own rate of return and replacement reserves, all of which conclusively shows said rate of 29½ cents is unjust, unreasonable, unlawful and confiscatory, all of which respondents will show if this application is allowed.

40

For the reason that said order of the Commission directing this respondent to reduce its rates is void and unenforceable because it is impossible for this respondent to [fol. 59] determine therefrom the amount of reduction so intended to be ordered.

41

For the reason that by making said order effective August 1st, 1932, and by directing this respondent to reduce its charges to its customers as of that date, respondent is placed in the position of guaranteeing the validity of said order and its final approval by the courts and in the event such order is, in the orderly course of such proceedings, determined to be invalid this respondent will have suffered the confiscation of its property during the entire period of litigation and will thereby suffer irreparable injury, respondent being informed and believing that the validity of said order will be contested in the courts.

42

For the reason that the finding of said Commission that there is a duplication in the services rendered by Henry L. Doherty & Company and by The Gas Service Company is without support in the evidence and is contrary to all of the evidence in regard thereto and is not true in fact.

43

For the reason that said Commission permitted to be introduced before it incompetent and irrelevant testimony and excluded from the evidence competent and relevant testimony offered by respondents and erroneously ruled upon

the several motions and objections made by the parties respectively during the course of said proceeding.

[fol. 60]

44

For the reason that said Commission, wholly without support in the evidence and in disregard of all evidence in relation thereto, eliminated from the valuation of the property of the Cities Service Gas Company as not used and useful the compressor stations at Hogshooter, Hominy and Owassa and refused to make any allowance whatever therefor.

45

For the reason that said Commission disregarded and ignored all evidence before it as to the going concern value of the Cities Service Gas Company, including the testimony of its own expert witness, and without any support whatever in the evidence arbitrarily reduced said item to an inadequate amount.

46

For the reason that said Commission arbitrarily and without any evidence in support thereof, eliminated the item claimed by respondents as cost of financing entering into the rate base of the Cities Service Gas Company.

47

For the reason that said Commission unlawfully and arbitrarily disregarded the evidence and misconstrued and misinterpreted the same as to all of the property accounts of the Cities Service Gas Company and all matters discussed in the original and reply briefs of the respondents and likewise with respect to the contracts between the several respondents and Henry L. Doherty & Company and for the reason that the findings of said Commission as to [fol. 61] the intangible items entering into the rate base of the Cities Service Gas Company are without support in the evidence and contrary to the evidence.

48

For the reason that said Commission in its said decision, opinion, findings and order exceeded its jurisdiction and undertook to determine strictly legal questions, jurisdiction

with respect to which is, by the Constitution of the State of Kansas, vested exclusively in the courts.

49

For the reason that in said decision, opinion, findings and order the several respondents are ordered to reduce their respective rates in an amount equal to ten cents per M. C. F. on gas sold by them for domestic purposes plus an amount equal to 1¾ per cent of their gross revenue, in which respect said decision, opinion, findings and order, and each of them, are beyond the jurisdiction of the Commission, impossible of performance and void for the following reasons:

A. Said reduction is required to include 1¾ per cent of gross revenue from the sale of industrial gas sold on special written contracts and at a price which returns to the respondents respectively said 1¾ per cent on said sales respectively, such industrial sales having nothing whatever to do with this investigation as to the reasonableness of the contract for the sale of domestic gas at the city gates and the inclusion in said reduction of 1¾ per cent of gross revenue from industrial sales in a reduction to domestic consumers is unreasonable, unlawful, unjust and void.

[fol. 62] B. The amount represented by 1¾ per cent of gross revenue is an amount impossible of determination in advance, varies monthly and is not a definite, fixed, or ever determinable amount to be taken into consideration in establishing a rate on August 1st, 1932, as directed.

C. The rates of the several respondents are of many kinds and types including the three-part rate of the Union Public Service Company in effect at Ottawa; the two-part rate of The Western Distributing Company in effect in some twenty small towns in the vicinity of Wichita; rates consisting of a service charge and a commodity charge such as the rates of Union Public Service Company at Paola, Osawatomie and other cities in that locality; and step or block rates such as are used by practically all respondents in some of the cities served by them; that even if the amount of the reduction so attempted to be ordered could be determined there is no direction in said order as to how such reduction should be applied to the rate in ques-

tion, that is, whether it should affect a service charge and if so to what extent; how it should be applied to a three or two part rate—whether to the service charge, the demand charge or the commodity charge or to all, and if to all, in what proportions; how it should be applied to a step or block rate whether in the first step or block, the second or some subsequent one or whether to all and if so in what proportion; for all of which reasons said decision, opinion, findings and order, and each of them, are meaningless, unreasonable, unlawful, not possible of performance and void.

D. Under the laws of Kansas an existing rate can be changed by the Commission only after a full and lawful hearing, the finding on proper evidence that existing rates are unreasonable, and the substitution of a definite rate by [fol. 63] the Commission for the rate so found to be unreasonable, none of which things were done herein.

E. Respondents have no statutory or other right to put in effect a rate not established or approved by the Commission and any rate it might attempt to put in effect under said order would neither be so established or approved.

F. For all, or a part of which, reasons it would be impossible for this respondent to comply with said order and the same is void.

50

For the reason that the reduction attempted to be ordered put in effect applies alike to all respondents, the same as if their present rates were based on gas at forty cents per M. C. F. at the city gate, whereas such is not the fact, instances of which are the rates of The Arkansas Valley Gas Company at Arkansas City, based on local gas at fifteen cents per M. C. F. at the city gate; the rates of The Hutchinson Gas Company at Hutchinson, based on local gas at twenty-five cents per M. C. F. at the city gate, the rates of Union Public Service Company, based on an average city gate rate of thirty cents per M. C. F. at Parsons, using both main line and local gas, and twenty cents per M. C. F. at Cherryvale, using all local gas; the rates of The Newton Gas Company at Newton, based on local gas at twenty-five cents per M. C. F., and the rates of The Western Distributing Company at El Dorado, based on

local gas at the city gate at twenty-five cents per M. C. F.; and the rates of the Pittsburg Gas Company in effect under an injunction of the District Court of Shawnee County prohibiting the interference of the Commission by the rate [fol. 64] attempted by this order or otherwise. For all of which reasons said order is unreasonable, unjust, discriminatory, unlawful and void and if intended to require an adjustment of rates on the basis of 29½ cents at the city gate would require an increase in rates in all cities where existing rates are based on a city gate rate of less than 29½ cents instead of a reduction; that the Commission must take judicial knowledge of the rates of this respondent, part of its official records, and of the applicability of said order in these several respects to it, separate and apart from all other respondents.

51

For the reason that in respect to the several matters called to the attention of the Commission in each and all of the foregoing paragraphs the action of the Commission deprives this respondent of its property without due process of law; denies it the equal protection of the laws; impairs the obligation of its contracts; undertakes to legislate with respect to interstate commerce and usurps the business management of the several companies involved, all in violation of the Constitution of the United States and the Constitution and laws of the State of Kansas and particularly Clause 3 of Section 8 of Article 1, the first subdivision of Section 10 of Article 1 of the Constitution of the United States and the Fourteenth Amendment thereto.

Wherefore, this respondent prays that said decision, opinion, findings and order be set aside and a rehearing granted it herein.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

[fol. 65] EXHIBIT "E" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts, and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Wichita Gas Company, Wichita, Kansas;
Hutchinson Gas Company, Hutchinson, Kansas;
Newton Gas Company, Newton, Kansas;
Pittsburg Gas Company, Pittsburg, Kansas;
Capital Gas & Electric Company, Topeka, Kansas;
Wyandotte Gas Company, Kansas City, Kansas;
Arkansas Valley Gas Company, Arkansas City, Kansas;
Girard Gas Company, Girard, Kansas;
Union Public Service Company, 43 towns;
Western Distributing Company, 27 towns;
Winfield Natural Gas Company, Winfield, Kansas;
Tri-City Gas Company, Kansas City, Mo.;
Gas Service Company, Kansas City, Mo.;
American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order Granting a Rehearing

Now, on this 5th day of August, 1932, the application of the respondents for a rehearing in the above entitled matter comes regularly before the Commission for final determination. The application contains fifty-one alleged grounds for a rehearing. After considering all of the allegations contained in the respondents' application, the Commission finds:

That all but one of the fifty-one grounds alleged by the [fol. 66] respondents in their application for a rehearing are without merit, and present no issues which were not fully considered by the Commission in the original proceedings.

That paragraph thirty-nine of respondents' application does present new matter and requires evidence which was not available at the time the original hearing before the

Commission was closed. That said paragraph thirty-nine of respondents' application for a rehearing goes to the decreased earnings of the Cities Service Gas Company for the year ending June 30, 1932, and should receive consideration by this Commission.

The Commission therefore further finds:

That a rehearing should be granted the respondents in the above entitled cause, and that the respondents should be given an opportunity to show the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

The Commission further finds that the rehearing should be set for ten o'clock, on August 15, 1932, at the offices of the Commission, in the State House, Topeka, Kansas.

The Commission further finds that the order issued on the 30th day of July, 1932, in the above entitled matter, should be suspended pending final determination of the matter on rehearing.

It is therefore, by the Commission ordered, That the application of the respondents in the above entitled cause be, and the same is hereby granted; that a rehearing be held at ten o'clock on August 15, 1932, at the State House, Topeka, Kansas, at which time the respondents will be given an opportunity to present evidence in behalf of their allegation as to the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

It is further by the Commission ordered that the order of this Commission issued on the 20th day of July, 1932, in [fol. 67] the above entitled matter, be, and the same is hereby, suspended, pending final disposition of the matter after the rehearing.

J. W. Greenleaf, Thurman Hill, Chas. W. Campbell.
Attest: Herman L. Gees, Secretary.

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[fol. 68] EXHIBIT "F" TO BILL OF COMPLAINT

The Wichita Gas Company

This respondent offers to show by the witnesses F. C. Hamilton and Fred H. Rice that the present value of its property used and useful in rendering service to its consumers in the city of Wichita, Kansas, is $2,872,854.00.

That its gross earnings for the year ending June 30th, 1932, were $1,818,850.00.

That for the year ending June 30th, 1932, it paid for purchased gas to the Cities Service Gas Company, from which it receives its entire supply, the sum of $1,175,116.00 at the rate of 40c per M. C. F. for domestic gas, of which it purchased 2,415,298 M. C. F.

That its operation and maintenance expense, exclusive of purchased gas, for said year ending was $462,638.00.

That the net earnings applicable to depreciation and return for said period were $181,096.00.

That the reduction in salaries effective June 15th, 1932, will result in a saving in operating expenses of $24,338.00.

That the earnings of the company for said year ending had said reduction in salaries been in effect during the entire period would have been $205,434.00, which would be a return of only 7.2 per cent on the present fair value of its property.

That the net earnings for said period reflect profit from sales to the Kansas Gas & Electric Company for a five months' period in the amount of $18,669.00; that this customer is no longer connected and the net earnings should be reduced by this amount in order to represent a normal year and would leave the net earnings $186,765.00 or 6.5 per cent of the present fair value of the property.

That the County Assessor of Sedgwick County, the local Board of Equalization and the State Tax Commission have [fol. 69] increased taxes of The Wichita Gas Company $1,000,000.00 over the amount returned by the company, which will result in an increase of taxes in the amount of $31,298.00, which should be deducted from the above net earnings in order to represent the future normal year which would reduce the net earnings of the company to $155,467.00 or 5.4 per cent on the present value.

The company is unable to procure gas at the city gate for less than the price now being paid; that existing rates do not permit said company to make a fair return on the fair value of its property and that the reduction in rates attempted to be ordered in the Commission's order of July 20th is unreasonable, unjust and would result in the confiscation of its property.

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[fol. 70] EXHIBIT "G" TO BILL OF COMPLAINT

Respondents offer to show by the witness A. W. Ambrose that he is Vice President and Assistant General Manager

of the Cities Service Gas Company; that he has been with said company since the year 1923; that prior thereto he was Chief Petroleum Technologist of the Bureau of Mines of the United States Government; that he is familiar with the gas reserves of Cities Service Gas Company, most of which were purchased under his direction and supervision; that in his opinion as an officer of said company they are all necessary in order to guarantee service to the consumers on said system; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas panhandle field was 1,263,000,000 feet per day, of which only 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oils, or blown in the air and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that said Commission now has under consideration an order limiting all takes from wells to five (5%) per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,257 acres allowed by this Commission will be wholly inadequate for even the coming winter, and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commission, [fol. 71] service will fail; that under present practices in Texas the owners of approximately ten (10%) per cent of the leases are producing approximately eighty-two (82%) per cent of the gas, none of which is connected to pipe lines or used by them; that such practices have reduced rock pressure in the Borger territory from the original 430 pounds to less than 50 pounds; that gas in the area, including the 71,267 acres allowed by this Commission is migrating to the low pressure Borger area; that the reserves of gas under said 71,267 acres are being thus constantly depleted and are not available to the Cities Service Gas Company as assumed by this Commission; that in its computa-

tion of proper reserves this Commission has included the open flow of wells transferred to Texoma, amounting to approximately 250,000,000 feet per day; that all of these matters are necessary to be taken into consideration in determining proper reserves and were not considered by this Commission as known by it; that the reserves of the Cities Service Gas Company are not in excess of proper reserves as recognized by the gas industry and as owned and held by other major pipe line companies; that none of the gas acreage now held by Cities Service Gas Company was bought or is being held for speculation.

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EXHIBIT "H" TO BILL OF COMPLAINT

Respondents offer to show by the witness H. L. Eastman that dry hole allowance of $12,000.00 per year is wholly insufficient, unjust and unreasonable for the reason that in 1930 Cities Service Gas Company drilled ten (10) dry holes at a cost of $174,748.00 and in 1931 drilled two (2) dry holes at a cost of $126,339.00; and it is impracticable to undertake any exploratory drilling for $12,000.00.

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[fol. 72] EXHIBIT "I" TO BILL OF COMPLAINT

Respondents offer to show by the witnesses Ed Warren, J. G. Dickinson and Ross M. Stumtz that they are each and all familiar with the cost of gas wells in the Texas panhandle territory; that the witness Ritchie, who testified for the Commission and whose testimony was adopted by it in its findings, never drilled a gas well in the Texas panhandle and was not familiar with such costs; that neither the Marland Oil Company or Continental Oil Company, successor to the Marland Oil Company, and with which the witness Ritchie was supposed to have attained his experience and knowledge, drilled gas wells in the fields concerning which Ritchie undertook to testify; that rotary drilling is not generally used in said fields for gas wells and that the cost of rotary wells is greater than the cost of wells drilled with standard tools.

EXHIBIT "J" TO BILL OF COMPLAINT

All Respondents

These respondents offer to show by the witnesses F. C. Hamilton and Fred H. Rice that the present value of their property used and useful in rendering service to their consumers in all of said cities is $15,326,298.00.

That their gross earnings for the year ending June 30th, 1932, were $7,092,398.00.

That for the year ending June 30th, 1932, they paid for purchased gas from all sources $4,517,230.00.

That their operation and maintenance expenses, exclusive of purchased gas, for said period were $1,909,935.00.

That the net earnings applicable to depreciation and re-
[fol. 73] turn for said period were $665,233.00 to be adjusted by the deductions shown in the offer for Wichita.

That had the present salary reductions been in effect for the entire period the operating expenses would have been reduced in the sum of $91,756.00 and the net earnings would have been increased to $756,989.00, or 4.9 per cent on the fair value of all properties.

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[fol. 74] EXHIBIT "K" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Company, Wichita, Kansas.
B. Hutchinson Gas Company, Hutchinson, Kans.
C. Newton Gas Company, Newton, Kansas.
D. Pittsburg Gas Company, Pittsburg, Kans.
E. Capital Gas and Electric Company, Topeka, Kans.
F. Wyandotte Gas Company, Kansas City, Kansas.
G. Arkansas Valley Gas Company, Arkansas City, Kans.

H. Girard Gas Company, Girard, Kansas.
I. Union Public Service Company, 45 towns.
J. Western Distributing Company, 27 towns.
K. Winfield Natural Gas Company, Winfield, Kans.
L. Tri-City Gas Company, Kansas City, Mo.
M. Gas Service Company, Kansas City, Mo.
N. American Pipe Line Company, Bartlesville, Okla.

## Opinion on Rehearing

The above investigation of the reasonableness of the contracts and charges made by holding companies to subsidiary companies of the Cities Service Company doing business in the State of Kansas, comes now before the Commission for final decision on rehearing.

[fol. 75] On the 20th day of July, 1932, the Commission issued an order in the above entitled matter in which it found that the payments made by the respondent companies to Henry L. Doherty & Company in the amount of one and three-fourths per cent of the gross revenues of the distributing companies were unreasonable and excessive; that 29.5 cents was the reasonable price to be paid to the Cities Service Gas Company by the respondents for main line town border gas, and that any amount paid in excess thereof was unreasonable.

The respondent companies filed an application for rehearing setting up fifty-one separate grounds therefor. After due consideration the Commission found that the only new matter presented in the application for rehearing was that set out in paragraph 39 of the application for rehearing, which claimed a decrease in the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

On the 5th day of August, 1932, the Commission granted the application of respondents for rehearing in order to give the respondents an opportunity to show earnings of the Cities Service Gas Company for the year ending June 30, 1932. The rehearing was held on the 15th day of August, 1932, at which time respondents introduced evidence and an earning statement as to the earnings of the Cities Service Gas Company for the year ending June 30, 1932. The company also asked for permission to introduce evidence to show that compressor

station spare parts had not been included in the inventories; that the Commission had made an error of $5,000,000 in calculating the annual depreciation requirements of the company; and that the Commission had included in its calculation of gas available for the use of the Cities Service Gas Company nine wells which had been [fol. 76] sold to the Texhoma Gas Company. These three items will be discussed in advance of the earnings for the year ending June 30, 1932.

## Compressor Station Spare Parts

While it appears that the company keeps strict accounting of its materials and supplies on hand in various warehouses located at points generally over the system, it failed to include in its books and accounts which purport to show the cost of materials and supplies on hand currently, some replacement or repair parts in compressor stations of the value of $119,275.

The testimony shows that these replacement and repair parts were present at compressor stations on September 1, 1931, and were not included in the book value of materials and supplies on hand at that date.

The Commission, therefore, finds that the fair value of the pipe line system at September 1, 1931, should be increased from $73,029,235 to $73,148,510 to take into account this material.

## Annual Depreciation and Replacement Reserves

The respondents introduced evidence on the rehearing to the effect that the Commission in calculating the annual depreciation and replacement reserve requirements had made an error of $5,000. In its original opinion, on page 132 of the typewritten copy, the Commission accepted the per cent allowances as claimed by the respondents and applied them to the present cost of reproduction as found by the Commission. By applying these percentages to the values which the Commission found, it calculated that the annual allowances for physical property would be $1,894,022, based on physical property values of [fol. 77] September 1, 1931. This was the figure used by the Commission in its calculation. The figure of $1,889,022

found on page 132 was a typographical error and not used by the Commission in its calculation. The proper result was, therefore, reached and the typographical error requires no adjustments in the Commission's final conclusions.

### Gas Reserves

Respondents contend that the Commission in its computation of probable reserves, has included the open flow of wells transferred to the Texhoma-Company amounting to 250,000,000 feet per day. On page 449 of the Transcript, Mr. Nesbit, the company's chief geologist, testified that the sixty wells owned by the company had an open flow of approximately one billion and a half cubic feet of gas per day. "The latest report I have happened to have a note on here, a billion five hundred thirty-two million six hundred twenty-five thousand.

Q. Sixty wells, I take it, that is there are sixty wells?
A. Yes, sir; we have sixty wells.
Q. This open flow was for sixty wells?
A. Yes, sir; I think that is correct" (Tr. 449).

It appears quite evident, therefore, that the amount of open flow used by the Commission in determining the gas available to the company was from the sixty wells owned by the company. If the open flow in that particular field were further reduced to 250,000,000 cubic feet per day the calculation of the Commission would not be materially affected.

### [fol. 78] Earnings for Year Ending June 30, 1932

During the rehearing in this case respondents introduced Exhibit 102, purporting to show the financial results of the operations of the pipeline system during the year ended June 30, 1932, in support of its contention that due to depressed economic conditions its earnings had decreased since this investigation was started and that it was no longer enjoying the prosperity of former years.

Page 1 of Exhibit 102 purports to show the net income during the year ending June 30, 1932, amounted to $7,861,516.85.

Included in expenses in arriving at this net income is an item of $52,297.13 representing payments to Henry L.

Doherty & Company under the 1¾ per cent contract and $50,000 rate case expenses. Deducting from expenses the payments to Henry L. Doherty & Company, for reasons elsewhere stated herein, and deducting the item of rate case expenses, because it is an abnormal nonrecurring item, results in net income before allowance for depreciation and depletion of $7,963,813.

After allowances are made for depreciation, depletion, amortization and dry hole expenses, aggregating $1,977,591, being the aggregate of such allowances found by the Commission based on September 1, 1931, value, results in a net income of $5,986,222.

The net income of $5,986,222 is equal to more than 8 per cent of the fair value of the pipeline system property at September 1, 1931, as found by this Commission, of $73,149,510.

The average net income during the year ended December 31, 1930, and the twelve months ended June 30, 1931, as heretofore found by this Commission, added to the net in- [fol. 79] come for the twelve-month period ended June 30, 1932, of $5,986,222 results in an average net income during these three annual periods of $6,769,936 which is equal to 9.87 per cent of the average value during these periods and 9.25 per cent of the value at September 1, 1931, of $73,148,510.

The net income before depreciation and depletion for the three annual periods were as follows:

| | |
|---|---|
| December 31, 1930 | $9,006,687 |
| June 30, 1931 | 8,889,565 |
| June 30, 1932 | 7,963,813 |

giving an average annual income over the three periods of $8,620,022.

The depreciation and depletion requirements for the three annual periods under investigation were as follows:

| | |
|---|---|
| December 31, 1930 | $1,776,881 |
| June 30, 1931 | 1,795,785 |
| June 30, 1932 | 1,977,591 |

Which results in an average annual depreciation and depletion requirement of $1,850,086, which subtracted from the average annual income before depreciation and depletion

gives us an average net income available for return on investment of $6,769,936.

The average town border main line gas sales during the three periods under investigation amounted to 20,560,450 M. C. F., which produces an average annual revenue of $8,138,523.

If this main line domestic gas were sold at thirty cents per M. C. F. it would have produced a revenue of $6,168,135, which would have resulted in a reduction in revenue of $1,970,388, this assuming that the 30-cent rate applied over the entire system—in fact it applies only to Kansas and therefore reductions in revenues would be much less [fol. 80] than $1,970,388; however, using the figures of $1,970,388, the net income available for return on investment would be $4,799,548. The average fair values during the three periods covered by the investigation were as follows:

| | |
|---|---|
| Twelve Months ending Dec. 31, 1930 | $66,296,147 |
| June 30, 1931 | 66,912,061 |
| June 30, 1932 | 73,148,510 |

Which results in an average value over the three periods of $68,785,573. The average net income during the periods covered by the investigation would have produced a rate of return of 7 per cent which the Commission has found reasonable in this investigation. The effect of the economies of the company put into practice since the investigation commenced by reducing administration expenses and paying less for gas should result in the company returning more than 7 per cent on the valuation fixed by the Commission.

In arriving at the determination as to what return may be expected, the Commission now has available the three annual periods. It is the belief of the Commission that a more accurate result is arrived at by considering the three annual periods than if the investigation had covered but one year. Consideration must also be given to the fact that the three years covered by the investigation have been years of economic depression and periods when the earnings of the company have been unusually low. The advantage of adopting a number of years as a test period was well expressed by Judge McDermott in the recent case of Denver Union Stock Yards Company v. United States, 57 F. (2d) 735, 752, in which he said:

"In arriving at a determination of what return may be expected of rates that are promulgated for the future, it is [fol. 81] proper to look to the experience of the past as a guide. For that reason, in all rate hearings, a test period is selected and a study made of the revenue and disbursements for that period. Ordinarily a test period of five years or more, if available, is selected. What the test period shall be depends on circumstances; for example, the years of the war are ordinarily excluded for the reason that such years are abnormal. Laying to one side such abnormalities, it is generally true that, the longer the test period, the more accurate the judgment for the future; the broader the base, the safer the estimate. When there has been a reasonably steady growth in the business, and reason to anticipate that it will continue, the factor of growth should be considered in estimating the future."

The Commission finds that consideration should be given to the decreased earnings and has made such adjustment by averaging the period in which the decreased earnings occurred with the other two annual periods under investigation.

The testimony during the rehearing of witnesses appearing for the respondents was to the effect that various operating economies had been inaugurated at about the close of the twelve months ending June 30, 1932, which will result in material reductions in expenses. The saving by reductions in wages and salaries alone will amount to approximately $104,000 per year, but this saving is reflected in the net income for the year ended June 30, 1932, for a period of only two weeks, the reduction having been effective beginning June 15, 1932.

For the purpose of comparing the net income of June 30, 1932, with a figure representing fair value, the Commission has used the fair values as heretofore found and has not given effect to any reductions which might be re- [fol. 82] quired in such values due to lowering of material and labor prices since the time of the valuation.

The financial position of the company at June 30, 1932, indicates that this system is enjoying a marked degree of prosperity in the face of generally otherwise depressed conditions. It reduced its indebtedness to its parent company from $9,000,000 at June 30, 1931, to $6,500,000 at June

30, 1932; it increased its replacement reserve from $10,818,020 at June 30, 1931; to $12,455,838 at June 30, 1932, even after absorbing deferred charges to the reserve, which have been carried as deferred charges on the balance sheet, to the extent of approximately $750,000. The company has a surplus of $7,852,103.40; it has reduced its current liabilities at June 30, 1932, compared with June 30, 1931, and was able to loan to affiliated companies and have owing it at June 30, 1932, from such affiliated companies $2,911,654.13.

A large part of the decreased earnings during the past year has been caused by loss of sales of industrial gas. This has decreased the earnings of the Cities Service Company in approximately $1,000,000. It is only reasonable to assume that industries will soon continue operation and that the loss of industrial sales will be only a temporary abnormal condition.

Evidence introduced at the rehearing disclosed that the respondents have reduced rates at the city gate and to the consumers in several cities in Kansas.

The domestic consumer should not be required to carry all of the loss in revenue from the industrial gas, but the company which has enjoyed prosperous years in the past should be willing to absorb a part of this loss during the abnormal time. The Commission is of the opinion that most of the gas pipeline companies, situated as is the Cities Service Gas Company, would be satisfied with a return, [fol. 83] under present conditions, of much less than 7 per cent. The Commission, therefore finds that 30 cents is a reasonable price to be paid by the respondent distributing companies purchasing main line town border domestic gas from the Cities Service Gas Company, and that anything charged in excess thereof by the pipeline company to the distributing plants is unreasonable.

The Commission further finds that under authority of Chapter 204 of the Laws of 1931, the costs of this proceeding in the sum of $66,936.08 should be taxed against the respondents.

An appropriate order will be issued in accordance with the findings in the original opinion as modified by this supplemental opinion on rehearing.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

Chairman Greenleaf dissenting in part.

After full consideration of all the facts in the case, including all the evidence submitted in the rehearing held in the Commission hearing room August 15, I am still convinced that the reasonable price to be paid for main line town border domestic gas to the pipeline company, by its affiliated distributing company at the city gate is 32 cents per 1000 cu. ft., and any amount above that price is unreasonable.

Jesse W. Greenleaf.

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[fol. 84] EXHIBIT "L" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Company, Wichita, Kansas;
B. Hutchinson Gas Company, Hutchinson, Kansas;
C. Newton Gas Company, Newton, Kansas;
D. Pittsburg Gas Company, Pittsburg, Kansas;
E. Capital Gas and Electric Company, Topeka, Kansas;
F. Wyandotte Gas Company, Kansas City, Kansas;
G. Arkansas Valley Gas Company, Arkansas City, Kansas;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kansas;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order

Now, on this 31st day of August, 1932, the above matter comes regularly before the Commission for final determina-

tion upon the application of respondents for a rehearing, which was limited by the Commission to ground thirty-nine in the motion of respondents, and the Commission finds:

[fol. 85] 1

That during the year ending June 30, 1932, there was a falling off of sales of respondents' domestic gas in the sum of approximately $400,000, as compared with the year ending June 30, 1931.

2

That certain economies put into effect by the respondents since June 1, 1932, will result in an annual savings of $104,000.

3

That since June 1, 1932, respondents are buying and attempting to buy field gas at 6 cents instead of 8 cents per M. C. F., and that this policy will also reduce operating expenses.

4

That with these savings deducted from the net earnings, the reduction in earnings for the next fiscal period should not be in excess of $300,000.

5

That it would be inequitable to accept this figure of reduction in earnings without taking into consideration that reproduction costs new at this time would also cut valuations fixed by the Commission in its original opinion substantially.

6

That the findings in the opinion in the above entitled matter signed on the 19th day of July, 1932, as supplemented by the opinion on rehearing, should be and hereby are incorporated in this order and made a part hereof.

[fol. 86] 7

The distributing companies, respondents above named, and the Cities Service Gas Company, are mere agents or instrumentalities of the Cities Service Company.

8

That the contract between Henry L. Doherty & Company and the various distributing companies, respondents above named, under which Henry L. Doherty & Company purports to render various departmental services to the distributing companies, and receives as consideration therefor one and three-fourths per cent of the gross revenues of the distributing companies; an engineering fee of five per cent of the cost of construction; a fee for services of the securities department and an additional expense and per diem charge is unreasonable, and that the compensation received thereunder is excessive to the extent of the payment of the one and three-fourths per cent of the gross revenues of the distributing companies.

9

That the contract between the Cities Service Gas Company, a natural gas pipe line company, and respondents above named, under which the Cities Service Gas Company sells gas to the distributing companies at the city gate at an average price of 39.5 cents per M. C. F. is unreasonable, and that the payments made thereunder are excessive above the amount of 30 cents per M. C. F. for such main line border gas.

[fol. 87]

10

That 30 cents is a reasonable price to be paid to the Cities Service Gas Company by the respondents for main line town border gas, and that any amount paid in excess thereof is unreasonable.

11

That the costs hereof incurred by the Commission herein, amounting to $66,936.08, should be taxed to and paid by the respondents.

12

That on and after the 1st day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payment made to Cities Service Gas Company for main line town border gas in excess

of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

It is therefore by the Commission ordered:

1

That on and after the 1st day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payments made to Cities Service Gas Company for main line town border gas in excess of [fol. 88] 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2

That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10:00 o'clock A. M., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable.

Thurman Hill, Chas. W. Campbell. Attest: Herman L. Gees, Secretary.

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[fol. 89] EXHIBIT "M" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company.

Part A. Wichita Gas Company, Wichita, Kansas;
B. Hutchinson Gas Company, Hutchinson, Kansas;
C. Newton Gas Company, Newton, Kansas;

D. Pittsburg Gas Company, Pittsburg, Kansas;
E. Capital Gas and Electric Company, Topeka, Kansas;
F. Wyandotte Gas Company, Kansas City, Kansas;
G. Arkansas Valley Gas Company, Arkansas City, Kansas;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 Towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kansas;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order

Now, on this 31st day of August, 1932, the Commission having found that 30 cents per M. C. F. is a reasonable price for the respondents above named to pay the Cities Service Gas Company for main line town border domestic gas, and that anything in excess thereof is unreasonable, [fol. 90] the Commission now has before it for consideration the question of determining the manner in which this reduction in expenses should be passed on to the consumer.

The Commission, therefore, finds that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, should charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer.

It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city

gate and 30 cents per M. C. F. and pass on this difference to the consumer.

By the Commission it is so ordered.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

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[fol. 91] EXHIBIT "N" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by holding Companies to Subsidiary Companies of the Cities Service Company

Application of The Wichita Gas Company for Rehearing on Opinion and Orders of August 31, 1932

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, applies for a rehearing in respect to all matters found and ordered and purported to have been determined here in by this Commission in its opinion and orders of August 31st, 1932, for the reason that said opinion, findings and orders, severally and collectively, are unlawful, unjust and unreasonable in the following respects and for the following reasons:

1

For all of the reasons set out in respondent's application for a rehearing on the opinion, decision, findings and order of this Commission of July 20, 1932, heretofore filed herein and granted by said Commission as to paragraph 39 only, all of the allegations of said original application for rehearing being again urged as against said opinions and [fol. 92] orders of August 31st, 1932, except the allegations of paragraph 39 thereof.

2

For the reason that in its ruling and decision on respondent's original application for a rehearing this Commission

wrongfully, unlawfully, unreasonably and unjustly granted said application as to paragraph 39 only and on the subsequent rehearing refused to permit respondent to introduce evidence with respect to all other matters alleged in said application.

3

For the reason that in its opinion, findings and orders of August 31st, 1932, on rehearing said Commission neglected and refused to find the value of the property of the Cities Service Gas Company used and useful in rendering the service in which it is engaged as of the time of said rehearing, and neglected and refused to determine the earnings of said company as of said time and unjustly, unlawfully and unreasonably undertook to determine the reasonableness of its contract with respondent for respondent's supply of gas at the city gate on the basis of a valuation and earnings averaged over a period of years notwithstanding the fact that the earnings of said Cities Service Gas Company for the year ending June 30th, 1932, as shown by respondent's evidence on rehearing, represented earnings on all of the property of said Cities Service Gas Company, there being no material additions or extensions to said system during said period the earnings upon which were not included in the earnings as shown to said Commission.

[fol. 93]

4

For the reason that the two orders issued by said Commission on August 31st, 1932, are inconsistent and in direct conflict with the other, said Commission in one order having directed respondent to appear before it on October 17th, 1932, to show cause why a reduction in its operating expenses should not be passed on to its consumers, and in the other having ordered a reduction in rates as of September 1st, 1932, the day after said order was issued, one of said orders by its terms putting in effect an immediate reduction of rates of respondent and the other order by its terms postponing any reduction in rates until after the reasonableness and justice of such reduction should be determined by said Commission after affording respondent an opportunity to be heard.

5

For the reason that in said opinion and orders of August 31st, 1932, said Commission increased the rate of 29½ cents per M. C. F. to be charged by the Cities Service Gas Company, as found in its opinion, findings and order of July 20th, 1932, only one-half cent per M. C. F., notwithstanding the fact that in its said opinion, findings and orders of August 31st, 1932, it found the earnings of the Cities Service Gas Company for the year ending June 30th, 1932, to have fallen off $1,000,000.00 on account of decreased industrial business and $400,000.00 on account of a decrease in domestic business, or a total of $1,400,000.00, and said increase of one-half cent per M. C. F. is entirely inadequate to compensate for said decreased earnings.

[fol. 94]

6

For the reason that in said opinion, findings and orders of August 31st, 1932, said Commission eliminated from the operating expenses of the Cities Service Gas Company an item of $52,297.13 representing payments to Henry L. Doherty & Company under a contract between it and said Cities Service Gas Company, said Commission having no jurisdiction over said Cities Service Gas Company or Henry L. Doherty & Company for said purpose.

7

For the reason that said Commission in its opinion and orders of August 31st, 1932, eliminated from the operating expenses of Cities Service Gas Company an item of $50,000.00 covering rate case expenses, said item being a proper item of operating expense to be included therein.

8

For the reason that said Commission in its opinion and orders of August 31st, 1932, did not increase the replacement reserves of the Cities Service Gas Company as previously allowed to correspond with the increased valuation found for its property.

9

For the reason that said Commission in its opinion and orders of August 31st, 1932, after finding that the earnings

of the Cities Service Gas Company had decreased $1,400,000.00 from the previous year, arbitrarily and capriciously found without any support in the evidence that such de-
[fol. 95] crease for the year ending June 30th, 1932, would be only $300,000.00.

10

For the reason that said Commission in said opinion and orders assumed that the value of the property of the Cities Service Gas Company at the time of said rehearing would be less than the value found by said Commission in its original opinion, findings and order without any evidence in support thereof.

11

For the reason that said Commission in said opinion and orders of August 31st, 1932, prohibited this respondent from setting up on its books any sums payable to Henry L. Doherty & Company under respondent's contract with it or to Cities Service Gas Company under its contract with it for purchased gas in excess of the price of 30 cents per M. C. F., said Commission being without authority to dictate the manner in which respondent's books should be kept.

12

For the reason that said Commission in its conduct of said proceeding has exceeded its jurisdiction and proceeded in direct violation of the limitations placed upon its jurisdiction by Chapter 239 of the Session Laws of 1931, wherein its jurisdiction is expressly limited to the determination of issues arising in a case the purpose of which is to "ascertain the reasonableness of a rate or charge to be made by a public utility."

[fol. 96] 13

For the reason that in its order of July 2nd, 1931, instituting Docket Number 13127 said Commission limited its investigation to the reasonableness of contracts made with and services rendered to subsidiary companies of the Cities Service Company by their various holding companies, said order expressly eliminating from the issues presented by said order the reasonableness of any contracts between subsidiary companies.

Wherefore this respondent prays that said opinion, findings and orders of August 31st, 1932, be set aside and a rehearing granted it herein.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

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[fol. 97] EXHIBIT "O" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Supplemental Application of the Wichita Gas Company for Rehearing on Opinion and Orders of August 31, 1932

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, files this supplement to its application for rehearing on the said opinion and orders of August 31, 1932, hereby calling to the attention of said Commission matters transpiring subsequent to the time said application for rehearing was filed herein.

In addition to all matters set out in former applications for rehearing filed herein, respondent alleges that on the 9th day of September, 1932, the duly constituted, regulatory body of the State of Texas issued an order, a copy of which is not yet available to respondent and cannot be hereto attached, but in which order said Commission restricted the takes of all wells to not more than four per cent (4%) of the potential capacity of such well or wells, or so much of such potential capacity as may be necessary to take care of current demands for domestic and industrial use, said order thereby making it impossible for the Cities [fol. 98] Service Gas Company to take from any wells drilled subsequent to the promulgation of said order in excess of four per cent (4%) of the potential capacity of such wells by reason of which all calculations of this Commission in its original opinion finding proper gas reservations

for said Cities Service Gas Company become erroneous and not applicable, and said allowed reserves become entirely inadequate, the same being based on the ability of said Cities Service Gas Company to take from all wells drilled on its allowed acreage twenty per cent (20%) of the open flow thereof.

For the further reason that the limitation and restriction so placed by the State of Texas on gas wells in said state makes necessary and essential to service all of the reservations owned by said Cities Service Gas Company and disallowed by this Commission.

Wherefore, respondent prays for a rehearing in accordance with its application filed herein.

Robert D. Garver, Robert Stone, Attorneys for said Company.

[File endorsement omitted.]

2

[fol. 99] EXHIBIT "C" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company, viz:

Wichita Gas Company, Wichita, Kan.;
Hutchinson Gas Company, Hutchinson, Kan.;
Newton Gas Company, Newton, Kan.;
Pittsburg Gas Company, Pittsburg, Kan.;
Capital Gas and Electric Company, Topeka, Kan.;
Wyandotte Gas Company, Kansas City, Kan.;
Arkansas Valley Gas Company, Arkansas City, Kan.;
Girard Gas Company, Girard, Kan.;
Union Public Service Company, 45 Towns;
Western Distributing Company, 27 Towns;
Winfield Natural Gas Company, Winfield, Kan.;
Tri-City Gas Company, Kansas City, Mo.;

Gas Service Company, Kansas City, Mo.;
American Pipe Line Company, Bartlesville, Okla.;
Respondents

Opinion by the Commission

The above investigation of the reasonableness of the contracts and charges made by holding companies to subsidiary companies of the Cities Service Company doing business in the state of Kansas comes now before the Commission for final decision.

Upon the 2d day of July, 1931, the Commission on its own motion ordered an investigation of such contracts and charges, and set down said matter for hearing upon the 18th day of August, 1931. Owing to the magnitude of the task and in order that the parties be given fair opportunity to present their evidence, the case was continued from time to time and the first evidence was submitted on October 16, [fol. 100] 1931. The hearing was closed February 16, 1932. During this time the Commission heard testimony for twenty-six full days and received 101 exhibits, some of the exhibits containing several thousand pages. This evidence was introduced by forty witnesses, and the evidence when finally transcribed consisted of 2,901 pages of testimony. After the completion of the case the Commission granted the respondents and counsel for the state time to prepare and submit original and reply briefs, and these briefs have been submitted to and considered by the Commission.

Three contracts are involved in the investigation:

1. The contract between the Gas Service Company and the various distributing companies, respondents above named, under which the Gas Service Company operates and manages the distributing companies and keeps some of their books, and charges to such distributing companies certain sums monthly, purporting to be each distributing company's share of the expenses of the Gas Service Company.

2. The contract between Henry L. Doherty and Company and the various distributing companies, respondents above named, under which Henry L. Doherty and Company purports to render various departmental services to the distributing companies and receives as compensation therefor 1¾ per cent of the gross revenues of the distributing companies, an engineering fee of 5 per cent of the cost of con-

struction, a fee for services of the securities department, and an additional expense and per diem charge.

3. The contract between the Cities Service Gas Company, a natural gas pipe-line company, and the various distributing companies, respondents above named, under which the Cities Service Gas Company sells natural gas to the distributing companies at the city gates for 40 cents per M c. f., and in some cases less. This is a day-to-day contract, and is not in writing.

The American Pipe Line Company and the Cities Service Gas Pipe Line Company are also natural gas pipe line companies, included in the investigation. They are owned and controlled by the Cities Service Company. The property of the Cities Service Gas Pipe Line Company is leased, managed and operated by the Cities Service Gas Company, and its property is included in this investigation as the property of the latter company. The American Pipe Line Company being a unit of the pipe-line system, its earnings, expenses and property are consolidated with that of the [fol. 101] Cities Service Gas Company. The pipe-line companies will, therefore, be referred to in this opinion as the Cities Service Gas Company.

In order to get a clear picture of the reasons actuating the Commission in making the order of investigation it might not be amiss to relate a short history of the development of the gas resources of the state of Kansas, and its consequent effect on the consumers. It has been more than fifty years since gas was first produced in Kansas. At that time the commercial possibilities of gas in Kansas was given little consideration because of the limited market. The first use made of the gas from the first well in Kansas was to illuminate, through the use of flambeau lights, a country dance platform in Miami county, Kansas. As further gas wells were discovered the commercial possibilities were realized; companies were formed to drill gas wells and distribute gas to the people of Kansas.

During the past thirty years various fields have been discovered throughout the state and have been developed by producing and pipe-line companies. During this period of time much was learned by the gas industry as to methods of producing gas, and also in distributing the product to the consumer. One of the pioneers producing and distributing gas in this state was the Kansas Natural Gas

Company. Its history was rather a turbulent one, and finally, after receivership, its properties passed into the hands of the Cities Service Company.

This pioneer company served a very useful purpose. Its history taught other gas companies the value of conservation methods in the production of gas, and that by improvement in pipe-line methods much waste could be prevented at savings both to the company and the consumer. These matters were thoroughly developed in 1923 and 1924, when the Commission of Kansas was called upon to fix a fair and reasonable gate rate for the Kansas Natural Gas Company which was then owned and controlled by the Cities Service Company. At that time it was disclosed that one of the reasons for the forty-cent rate was the loss sustained from leakage. It was disclosed that the company lost a substantial part of the gas through this type of waste from the time the gas left the well until it reached the burner tip. It was further shown that the gas reserves at that time were problematical, most of the gas coming from shallow fields whose life expectancy was short and uncertain, creating a limited supply. This limited supply caused this company and other like companies to obtain large sums of money for the purpose of trying to find other sources of gas reserves to supply its consumers. These items just [fol. 102] related were factors which undoubtedly moved the Commission to approve the forty-cent rate as a proper charge paid by distribtuing companies to the main pipeline companies.

Since the last investigation of pipe-line rates in 1923 by this Commission, there has been a most radical change in the natural-gas industry. At that time most of the gas supply was used locally. Enormous gas reserves have since been developed and pipe-line construction practices have been advanced, so that it is possible without appreciable waste to transmit gas over long distances. The conditions then existing which in order to conserve the gas supply required the restriction of sale of gas to domestic consumers, principally for cooking purposes, no longer exists.

The general trend of all prices since 1923 has been downward, in fact the existing level of prices in a number of instances is lower than at any time in the past fifty years.

The Commission recognized these changing conditions and believed that such change required a redetermination of the reasonableness of the forty-cent gate rate.

## Jurisdiction

The Commission took jurisdiction of the investigation on the theory that services rendered and gas furnished by holding or affiliated companies were proper matters for consideration by the Commission in considering the reasonableness of rates of subsidiary or affiliated distributing companies, and that the reasonableness of the contracts, under which the holding or affiliated companies render service and furnish gas to the affiliated or subsidiary companies, is properly measured by the cost of service rendered and the cost of furnishing the gas.

The Commission finds from the undisputed evidence of the respondents that for all practical purposes Henry L. Doherty, doing business as Henry L. Doherty and Company, controls the voting power of the Cities Service Company.

The evidence also clearly discloses that all of the fiscal agency contracts under which Henry L. Doherty and Company is paid 1¾ per cent are made between Henry L. Doherty and Company on the one part and the directors of the subsidiary companies on the other part; that the common stock of the subsidiary or distributing companies is held by the Cities Service Company and that Henry L. Doherty and Company, having control of the Cities Service Company, has control of the election of the officers and directors of the subsidiary companies with which he contracts (Tr. 1679).

[fol. 103] Henry L. Doherty, individual, appoints the general auditor of Henry L. Doherty and Company. "With the general auditor, the directing head of these activities, rests the appointment or removal of secretaries and others in responsible positions in the office of all the Cities Service subsidiaries." (Ex. 11, p. 6.)

The common stock of the following distributing companies, respondents herein, is owned by the Gas Service Company with the exception of the directors' shares: Arkansas Valley Gas Company, Capital Gas & Electric Company, Girard Gas Company, Hutchinson Gas Company, Newton Gas Company, Union Public Service Company, Pittsburg Gas Company, Western Distributing Company, Wichita Gas Company, and Wyandotte County Gas Company. (Ex. 28.)

All of the common stock of the Gas Service Company, except qualifying directors' shares, is owned by the Cities

Service Company. Therefore, all of the common stock, with the exception of directors' shares of all the distributing companies, respondents herein, is owned and controlled by the Cities Service Company through its control and ownership of the Gas Service Company.

The common stock of the Cities Service Gas Company, which sells gas at the city gates to distributing companies now under investigation, with the exception of the directors' shares, is owned by the Empire Gas & Fuel Company. (Ex. 28.) All of the capital stock, with the exception of the directors' shares, of the Empire Gas & Fuel Company is owned by the Cities Service Company.

All of the stock of the Cities Service Gas Pipe Line Company and the American Pipe Line Company, except qualifying directors' shares, is owned by the Cities Service Company. (Ex. 28.)

It is, therefore, apparent that the common stock of all the distributing companies and all the gas pipe-line companies which sell them gas is through intercorporate relations owned and controlled by the Cities Service Company, and the voting power of the Cities Service Company is in turn controlled by Henry L. Doherty and Company.

The relationship of the companies are such that the same principles will apply to all companies involved in the three contracts under investigation and they need not be treated separately.

At the time this hearing began there was some dispute as to the right of the Commission to inquire into the reasonableness of these contracts. The case of the Western Distributing Company v. The Public Service Commission was [fol. 104] then before the United States supreme court for decision. There was a controversy between counsel for the gas companies and counsel for the Commission as to whether or not the authority of the Public Service Commission to make such investigation had been definitely established by the United States supreme court in the case of Smith v. Illinois Bell Telephone Company. (282 U. S. 133.)

The Western Distributing Company case has now been decided by the United States supreme court and this question has been definitely determined. In that case the court said:

"Having in mind the affiliation of buyer and seller and the unity of control thus engendered, we think the position of the appellees is sound, and that the court below was right in holding that, if appellant desired an increase of rates, it was bound to offer satisfactory evidence with respect to all the costs which entered into the ascertainment of a reasonable rate. Those in control of the situation have combined the interstate carriage of the commodity with its local distribution in what is in practical effect one organization. There is an absence of arms' length bargaining between the two corporate entities involved, and of all the elements which ordinarily go to fix market value. The opportunity exists for one member of the combination to charge the other an unreasonable rate for the gas furnished, and thus to make such unfair charge in part the basis of the retail rate. The state authority whose powers are invoked to fix a reasonable rate is certainly entitled to be informed whether advantage has been taken of the situation to put an unreasonable burden upon the distributing company, and the mere fact that the charge is made for an interstate service does not constrain the Commission to desist from all inquiry as to its fairness. Any other rule would make possible the gravest injustice, and would tie the hands of the state authority in such fashion that it could not effectively regulate the intrastate service which unquestionably lies within its jurisdiction.

"The principles applicable in a rate investigation, where similar corporate relationship existed, were recently announced in Smith v. Illinois Bell Telephone Co., 282 U. S. 133, 152, 153, 51 S. Ct. 65, L. Ed. 255, and no purpose would be served by repetition or elaboration of what was there said." (Western Distributing Company v. Public Service Commission, 252 S. Ct. 283.)

The right of a public service commission to inquire into the cost of service rendered and gas furnished by holding or affiliated companies in determining the reasonableness of the contract is now definitely established and requires no further discussion. That is true regardless of the interstate feature of the business.

The Commission is given authority under R. S. 66-110 and R. S. 66-111 to investigate on its own motion any regu- [fol. 105] lation, classification, practice or act of a public

utility, and by R. S. 66-113 is given authority to substitute a correction therefor after such hearing and investigation, if necessary.

## The Gas Service Company Contract

This is a contract between the Gas Service Company and the various distributing companies owned and controlled directly by the Gas Service Company through stock ownership. The various distributing companies own one or more, and in some instances many, operating or distributing units. The contract is made between the Gas Service Company and the distributing companies, and the latter companies are allocated a proportion of the expenses of the Gas Service Company, which purports to be the actual expenses of that company in performing the various services for the distributing companies and their operating units.

Under the contract the Gas Service Company agrees to perform certain departmental activities. For this purpose departments are maintained consisting of accounting, auditing, new business, budget, purchasing, stores, insurance, rate and valuation, legal, engineering and operating, and news functions. (Ex. 12.)

There is no dispute that services are rendered by the various departments of the Gas Service Company. All the expenses of the Gas Service Company arising from the various departments are allocated to the properties, in some instances on a customer basis in the proportion that the number of customers of each property bears the total number of customers, and in others on the basis of the relation of the revenue of each company to the aggregate revenue of all and not on the basis of services actually performed.

The Kansas City Gas Company and the Wyandotte County Gas Company do not participate in all expenses, but only in executive telephone and telegraph expenses, taxes, rent, department salaries and new business administrative expenses. The Capital Gas and Electric Company participates in all expenses except general clerical salaries, rents, welfare expenses, auditing expenses, warehouse expenses and general office supplies and expenses. The three companies above named maintain their own departments which perform the services covered by the expenses in which they do not participate.

The total expenses allocated by the Gas Service Company to all the distributing companies for the year ending June 30, 1931, amounted to $292,919.96. The Commission's ac-
[fol. 106] countants found upon examining some of the records of the Gas Service Company that there had been included in the total of $292,919.96, items aggregating $28,-972.56, which the Commission's accountants believed were not proper items of expenses to be charged against the distributing companies. The respondents thereupon prepared corrected exhibits in which the amount of expenses claimed for the year ending June 30, 1931, was reduced to $263,947.40.

These disputed items, aggregating $28,972.56, included items of legal expenses, traveling expenses, donations, memberships, subscriptions, miscellaneous expenses and incidental expenses pertaining to public relations.

The allocated expense for the year ending December 31, 1930, was submitted, and items of the same nature were questioned by the accountants for the Commission as were those submitted in the report for the year ending June 30, 1931. The controverted expenses amounted to approximately 10 per cent of the total allocated expenses.

For the purpose of eliminating any dispute and for the purpose of eliminating the necessity of a hearing upon each of the controverted items, the respondents agreed to the elimination of the expenses rejected by the accountants for the Commission.

In addition to the expenses allocated to the companies in the amounts recited above, expenses were charged directly to the distributing companies by the Gas Service Company. Such expenses charged directly to the distributing companies amounted to $101,869.78 during the twelve months ending June 30, 1931. After elimination of the disputed items the Commission does not find the amounts paid under the contract unreasonable.

The evidence discloses that under the contract the general ledger and other general books of the distributing companies are kept in Kansas City, Mo., contrary to the laws of the state of Kansas. (R. S. 17-616.) The Commission does not place any approval upon these contracts or this practice; the Commission will from time to time, as necessary, approve or disapprove any expenses which any of the distributing companies incur by reason of any services

performed by the Gas Service Company for them when credit for such expenses is claimed in rate proceedings by the distributing companies.

[fol. 107] The Henry L. Doherty and Company Contract

Henry L. Doherty and Company is Henry L. Doherty, an individual doing business as Henry L. Doherty and Company. The contract between Henry L. Doherty and Company and the various distributing companies under which Henry L. Doherty Company is paid 1¾ per cent of the distributing companies' gross revenue, an engineering fee equal to five per cent of the cost of construction, a fee for the services of the securities department, and in addition is paid the expenses, disbursements and per diem charge for Henry L. Doherty and Company's representatives while at the properties of the distributing companies, or traveling for them on special matters is as follows:

"To the Board of Directors of (the distributing company):

"GENTLEMEN: The undersigned, as fiscal agent, hereby offers to continue to place at the service of your corporation, under the same terms and conditions as have been in effect for the past several years, a complete organization which has been built up in connection with the operation and development of public utility, oil and natural gas properties, making available to you the combined experience, advice and assistance of this organization to aid you in solving such problems as may arise in connection with the conduct of your business. Among others, it is proposed to perform for your corporation, subject to the direction and control of your board of directors, the following service:

"I. Personnel. In so far as your corporation may desire, it is proposed to supply you with experienced executives and operators necessary for your business.

"II. Executive Service. Our staff of executives, financial advisers, engineers and accountants will advise and assist in franchises, rates, matters of public relations, and all matters of insurance, supervise expansion of territory and business, acquisition of additional properties, etc.

"III. General Accounting Services. Our accounting department will periodically audit the books of your corporation and generally advise in accounting problems and in

the development in accounting practices and procedure, and furnish the services of certified public accountants where special audits are required.

"IV. Statistical Services. Our statistical department will supply comparative statements of operating results of the various companies under our supervision and will also supervise or furnish statistical reports to financial institutions, government bureaus, and similar organizations.

"V. Purchasing Services. We will give you the benefit of the services of our purchasing department with regard [fol. 108] to the purchase of equipment, supplies, generally advise as to the desirable equipment, etc.

"VI. Designing and Construction Engineering. Our engineering staff will be available at all times to carry out all preliminary investigations requisite to determining the advisability of any proposed construction, will check the details of engineering design, perform engineering work where requested, and generally check the efficiency of your plant.

"VII. Financial Services. The financial department will provide plans for financing and for funds for capital requirements, including construction and additions to properties and acquisition of new properties; for the refunding of maturing obligations; will act as paying agent for coupons and dividends, and assist in the arranging of bank loans. Also, the financial department will furnish your corporation with a budget system for the advanced determination of financial requirements and operating results.

"VIII. Securities Department. The securities department will provide plans for the sale and distribution of various securities, and will formulate and carry out campaigns for sales under customer ownership plans, etc.

"IX. Valuation. The valuation department will, when required, prepare inventories and appraisals of property, and will advise as to experts who may be required to testify in valuation cases, and will generally assist in the preparation of the same.

"X. Tax Department. The tax department will prepare or supervise the preparation of federal and other tax returns and generally keep in touch with taxation problems.

"XI. New Business Department. The new business department will serve in the purchase and sale of appliances and equipment for resale, the determination of sales pol-

icies, promotion programs and sales personnel, in research and laboratory tests on domestic appliances, etc.

"XII. Technical and Research Department. The technical and research department will furnish a consulting service on all technical problems encountered by your corporation.

"Compensation. For the above services your corporation will pay as follows:

"1. A management fee equal to one and three-fourths per cent (1¾%) of its gross revenues, after deducting intercompany sales for resale.

"2. An engineering fee equal to five per cent (5%) of the cost of construction.

"3. For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made.

"In addition, your corporation will pay the expenses, [fol. 109] disbursements and reasonable per diem charges for our representatives while at the properties of your corporation or traveling for it on special matters.

"The agreement will take effect as of September 1, 1929, and shall continue in effect for a period of one year thereafter and shall be automatically renewed from year to year unless terminated by either party upon written notice to the other, mailed at least ninety days prior to the end of any year.

"A resolution adopted by your board of directors, authorizing the acceptance of this offer, shall constitute acceptance thereof.

"Yours very truly, (Signed) Henry L. Doherty and Company, by Ernest H. Johnson."

In considering the reasonableness of this contract, it will be well to compare it with the contract of the Gas Service Company. A comparison discloses that the same services are contracted to be performed by both companies. The services to be performed under the Gas Service Company contract are as follows:

1. Furnish all administrative and executive service.
2. Financial aid and advice.

3. Purchasing and warehousing.
4. Engineering and operating supervision.
5. All legal services.
6. All insurance purchasing.
7. All general accounting and reports.
8. Supervision and handling of all tax matters.
9. Handling of all pay rolls.
10. Making of all audits and auditing reports.
11. Make all governmental and regulatory commission reports.
12. Supervision of all new business operations.
13. Make all vouchers and disburse funds.
14. Supervise and direct all public relations work.
15. Do all general and policy advertising.
16. Make all valuations and rates and handle all matters pertaining to rate litigation, and routine matters with regulatory bodies.
17. Make and follow up all construction and financial budgets.

If any service is performed by Henry L. Doherty and Company under the Henry L. Doherty and Company contract, it must necessarily duplicate the service to be performed under the Gas Service Company contract. This duplication of proposed service is shown, also, by a comparison of exhibit 11, which is a summary of the activities to be performed by the departments of Henry L. Doherty and Company, with exhibit 12, which is a summary of the activities to be performed by the Gas Service Company, for which services the distributing companies fully compensate the Gas Service Company.

[fol. 110] The evidence also discloses that a number of companies are operated by Henry L. Doherty and Company at 60 Wall street, which in no way, so far as the evidence shows, contribute to the defraying of the expense of the operation of Henry L. Doherty and Company.

For example: The Gas Securities Company is owned by Henry L. Doherty and Company and has its office at 60 Wall street. The company has net assets of $23,252,907. The net earnings of this company for 1929 amounted to $1,960,376. (Tr. 1650.) The witness for respondents did

not know whether any payments were made by this company to Henry L. Doherty and Company. (Tr. 1651.) No revenue is shown from this source in exhibit 16.

The Gas and Electric Securities Company is owned by Henry L. Doherty and Company and has its office at 60 Wall street. This company has net assets of $24,932,188. Its income for the year 1929 amounted to $2,086,069. (Tr. 1652.) This company is operated by Henry Doherty and Company. (Tr. 17459) Exhibit 16 shows no revenue is obtained for its operation by Henry L. Doherty and Company.

Other companies are operated by Henry L. Doherty and Company which produce no revenue for it or contribute to its expenses, including the Doherty Securities Company, the Cities Service Securities Co., which is located at 60 Wall street and has on its payroll at times between 500 and 600 employees, the Doherty Organization Investment Company, and Henry L. Doherty and Company, Inc., and so forth.

Time and space will not permit a detailed discussion of the purported activities of each department as described in Exhibit 11. Generally, the departments' activities relate principally to the purchase and sale of stock of the Cities Service Company and other companies. As an example there is a transfer department with 355 employees, which may be discussed as illustrative of some of the activities of Henry L. Doherty and Company.

The Transfer Department is composed of three sections with a personnel of 355 and the sections include:

1. Transfer Division.
2. Ledger Division.
3. Reinvestment Division.

The Transfer Division. All the Cities Service Company and subsidiaries stock, bonds and debentures are issued and transferred in this division and Henry L. Doherty [fol. 111] and Company act, not only as transfer agent for Cities Service Companies, but also for subsidiary companies such as Public Service Company of Colorado, Ohio Public Service Company, Toledo Edison Company, Arkansas Natural Gas Corporation, Indian Territory Illuminating Oil Company, and others.

In this division considerable care must be exercised in transferring securities from one owner to another. All cases involving lost and stolen securities are handled by this division and their replacement is made only after satisfactory corporate requirements are complied with.

In this division at present, approximately 120,000 certificates are transferred and issued each month.

The Transfer Division maintains a close relationship with banks and trust companies which act as cotransfer agents, registrars and trustees of many security issues of the Cities Service Company. "This division has many interesting cases presented to it in connection with stolen securities and securities obtained through fraud, as well as cases where the transfer of securities involves estates, trustees, etc."

The Ledger Division is the division in which all stockholders' ledgers are maintained and dividends distributed to stockholders. The principal stock issues maintained in this division are Cities Service Company Common, Preferred "B" and "BB" and Cities Service Power & Light Company, on which monthly dividends are paid; also other issues such as Arkansas Natural Gas Corporation, Indian Territory Illuminating Oil Company, etc.

This division also maintains stockholders' records of subsidiary companies and records carrying the names and addresses of bond and debenture holders who have registered their bonds as to principal, or principal and interest. On fully registered bonds the interest is disbursed by this division.

This division carries approximately 60,000 stock and bondholders' accounts and pays monthly dividends and interest to more than 500,000 each month. As a dividend disbursing agency, the work of this division is more complicated than the average department of this kind because monthly cash dividends are paid in addition to monthly stock dividends.

In this division the Cities Service Company common stockholders' stock dividends are sold each month in cases where an all-cash dividend is desired. "Practically the entire force of this division is engaged in working on the [fol. 112] stockholders' ledgers for the first fifteen days of each month. Then the books are closed for dividends and the balance of the month is consumed in getting out the dividends."

In the Reinvestment Division stock dividends are accumulated and cash dividends reinvested in either Cities Service Company common or preferred stock, and this division also accrues the dividends where Cities Service Company common stockholders own less than twenty shares. This reinvestment division carries approximately 370,000 accounts for stockholders for whom Henry L. Doherty and Company are either accruing dividends, reinvesting cash dividends or accumulating stock dividends.

The Cities Service Company and its subsidiaries maintain more than thirty transfer agencies and registrars throughout the United States, and the transfer department is in contact at all times with the agencies as well as with the trustees who act in connection with such bond and debenture issues.

Other activities of the transfer department relate to stockholders' lists and proxies for stockholders' meetings, rights of stockholders, conversions and exchange of debenture and bonds for stock.

Another important department is the commission department. It maintains detailed records necessary to the proper functioning of the securities department in the promotion and sale of the securities of the Cities Service Company and its subsidiaries. It has a personnel of 108 people and consists of two divisions, namely, the commission division and the reports division.

The commission division keeps records of various securities delivered against sales made through the various sales agencies of the securities department and passes on the validity of claims for commissions based on such sales and authorizes payment of commissions. It also authorizes the charge-back from time to time of such commissions as have been paid out but have not become earned.

The duties of the reports division are to make payments or to charge back commissions upon advice from the commission division and to supply itemized listings of the items on which commissions are being allowed or charged back as well as commission statements carrying the cash payments or charge-backs. It maintains accounts for the various salesmen and securities dealers to which are posted the earnings reflected by the commission's statements and the cash payments of commissions.

This division supplies the securities department, from detailed information supplied by the commission division, various statistics and reports of sell-outs, placements, etc., [fol. 113] of the various securities. The enormous activity of this department as connected with securities sales can be visualized when the statement is read, on page 22 of exhibit 11, that its duties are performed in connection with the sales activities of approximately 1,200 retail salesmen, 15,000 employees of underlying companies and 600 dealers, all engaged in the sale of Cities Service Company stock.

The office service department has a personnel of 229. It handles addressograph records of security holders for the monthly run of dividend checks and other forms in connection with stockholders ledgers. The addressograph files include approximately 700,000 plates representing security holders of the Cities Service Company, stock salesmen, employees, et cetera. About 290,000 checks and 1,000,000 statements, envelopes, and forms are turned out each month. The monthly output of graphotype machines average 40,000 names, addresses and money amount plates. Between 6,000 and 7,000 changes of addresses of security holders are required each month.

Another important department is the security holders service bureau. This bureau was created in 1923 in the interest and for the benefit of the fast-growing numbers of holders of securities of the company. (Page 65, Ex. 11.)

It has normally a staff of twenty-six, including:

Representatives who greet visiting bond and shareholders and answer their many and telegraphic inquiries.

Investigators who make careful investigation and analysis of complaints and prepare figures and facts for reply to specific questions.

Stenographers and file clerks to type and file the correspondence and records of the bureau.

The principal feature of the greeters' bureau relates to inquiries and problems of individual shareholders and bondholders of the companies' securities who visit, write or telephone to the bureau for information, advice and help, and also to afford the securities holders a channel of direct personal contact with the company and its activities.

Some idea of the vast magnitude of the operations of this department and the expense connected therewith is reflected in the statement, on page 65 of exhibit 11, that

each month since the creation of the bureau it has answered approximately 5,000 letters, and its "greeters" have greeted in its office between 1,500 and 2,500 security holders each month in addition to answering local and long distance telephone calls to the extent of many hundreds daily.

[fol. 114] The bureau cares for the correcting and changing of addresses of holders, for reregistration of securities, advice to holders of special privileges, investigates claims of nonreceipt of dividend checks, receipts, etc., cares for emergency measures to safeguard temporarily holders of lost securities until duplicate certificates may be issued, investigates complaints from shareholders and bond holders who may have given their securities to brokers or dealers who may not be responsible, and assist in means of recovery.

The bureau advises and assist in the matter of transfer of certificates in estate settlements which are apt to be complicated; secures information on outside corporations for Cities Service stockholders and furnishes security holders with literature especially prepared by the bureau for the enlightenment of the Cities Service Companies' security holders.

Other departments include foreign oil department, marine and tank car activities, oil production and pipe line department, and oil refining and marketing divisions. These departments have no relation to, nor can they be of any service to, the natural gas distributing companies.

A natural gas department and geological department may be of service and value; however, the evidence shows that Henry L. Doherty and Company is paid directly and specifically for any services of any of its employees while out engaged on work for the gas companies at a per diem rate plus expenses.

Other departments consist of an accounting department, payroll department, et cetera, whose services naturally depend upon the functions of other departments.

There is a department called "functions of finance" whose activities are related to securing capital, arranging loans and furnishing collateral when necessary. The cost of furnishing capital by the sale of securities of underlying companies is covered in the management contract as follows:

"(3) For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made."

The Commission finds that the operations of Henry L. Doherty and Company are of no benefit to the distributing or pipe-line companies, except to the extent that any specific services may be rendered for which Henry L. Doherty [fol. 115] charges and collects specifically. The analysis of exhibit 11, setting out departmental activities of Henry L. Doherty and Company, shows that the contact of Henry L. Doherty and Company with the distributing companies is largely for the sole benefit of the holding company, the Cities Service Company.

An examination of the departmental activities of Henry L. Doherty and Company discloses that they are largely devoted to the purchase and sale of Cities Service Securities and details relating to the handling thereof. The Cities Service Company must pay the expense of its operation. It is not a proper charge to the expense of the subsidiary companies.

The evidence presented in this investigation as to the 1¾ per cent fee paid to the holding company by the subsidiaries discloses a modern corporate practice that should be frankly condemned. It is a scheme to take the cream from the gross earnings of the operating companies, leaving them the skimmed milk for sustenance. The money so taken for which no service is returned, may at times be the money needed to sustain the operating company—it may mean the difference between solvency and bankruptcy. This unearned money is filched from the pockets of the consumers, does not go to the stockholders, and unjustly enriches the management company. It is an immoral, if not illegal, dishonest corporate practice and will not be tolerated, much less approved by Public Service Commissions.

It further appears that any additional contact of Henry L. Doherty and Company with the distributing and pipeline companies is for the purpose of keeping Henry L. Doherty informed as to their activities and for the protection of his investment rather than for a direct benefit to the distributing and pipe-line companies. It also ap-

pears that the departments of Henry L. Doherty and Company are devoted to the extension of the investments of the Cities Service Company and Henry L. Doherty and Company, such as oil developments and others which in no way result in a benefit to the existing operating companies.

It appears that the activities of Henry L. Doherty and Company are a burden to the distributing and pipe-line companies rather than a benefit, in view of the fact that they must immediately transfer all their receipts to Henry L. Doherty and Company, leaving them dependent upon it for financial assistance for which they must pay, while Henry L. Doherty and Company has the benefit of these [fol. 116] receipts and the use of the funds of the underlying companies pending their distribution as dividends.

The relations between Henry L. Doherty and Company and the distributing and pipe-line companies places a further burden upon them due to the fact they must pay Henry L. Doherty and Company five per cent of the cost of their construction projects regardless of the benefit received or the services performed. Although this does not enter into the expense in determining a rate to be charged the consumer, it does affect the financial stability of the distributing and pipe-line companies.

The distributing and pipe-line companies, because of their relations with Henry L. Doherty and Company under this contract, have a further burden of carrying the operating expense of Henry L. Doherty and Company's securities holding companies, which were not shown to contribute to the departmental expense.

Further, because of the authority given Henry L. Doherty and Company as fiscal agent under the contract, the distributing companies are not left free to deal independently for the purchase of gas at the lowest possible price, it being the desire of Henry L. Doherty and Company to sell the pipe-line gas of its own company.

The test of the reasonableness of this contract as it relates to the 1¾ per cent payments thereunder, is to be determined by whether or not any services are actually performed for the benefit of these companies for which the companies are not billed specifically and, if so, what it costs Henry L. Doherty and Company to render this service.

There is no evidence in the record of any specific services having been performed for any of these companies by Henry L. Doherty and Company for which Henry L. Do-

herty and Company was not paid on a per diem basis and for its expenses. Practically all of the services which Henry L. Doherty and Company under its contract stands ready to perform, the evidence shows, was in fact performed by the Gas Service Company, and that the Gas Service Company was paid by the distributing companies for this service.

The evidence shows that Henry L. Doherty and Company is amply compensated for any services rendered these companies by the engineering fee, by the payment of a fee to be mutually agreed upon for services rendered by the securities department and for the direct payments for specific services performed.

From all which the Commission concludes that the fiscal [fol. 117] agency contracts between Henry L. Doherty and Company and the respondent distributing companies and the pipe-line companies are unreasonable and the amounts paid thereunder are excessive to the extent of 1¾ per cent paid on the gross receipts of these companies.

## The Cities Service Gas Company Contract

This is the contract between the respondent distributing companies and the Cities Service Gas Company, under which the distributing companies purchase natural gas from the pipe-line company at the city gates. The contract is a day-to-day agreement and not in writing. In most cases the price contracted to be paid is forty cents per M. c. f. In some instances the price is lower. The average price for main line domestic gas is 39.5 cents.

The reasonableness of the contract is to be tested by what it costs the Cities Service Gas Company, the natural gas pipe-line company, to furnish gas to the affiliated distributing companies, and the rate of return earned by it on the fair value of its property used and useful in this service. This will involve a consideration of the following factors:

1. The fair value of the pipe-line system used and useful in service, exclusive of gas leases.
2. The present fair value of the gas leases, used and and useful.
3. A proper allowance for annual depreciation and depletion.

4. The net earnings of the company available for annual return.

5. The fair rate of return.

These factors will be considered in the order set out above.

## The Fair Value of the Pipe-line System Used and Useful in Service

In arriving at the value of the pipe-line system used and useful in service, the Commission has the valuation submitted by Mr. Hamilton, engineer for the respondents, the testimony of Mr. Eastman in support of Mr. Hamilton's exhibit, and the valuation submitted by Mr. Black, the engineer for the Commission.

Both Mr. Black and Mr. Hamilton have followed the same classification of accounts, but it is possible that some property classified by Mr. Black under Account 1314, Production field-line equipment, may have been classified by Mr. Hamilton under Account 1333, Transmission-line equipment, or vice versa. Mr. Black classifies certain rights of way under Account 1307, Production rights of way, whereas Mr. Hamilton shows nothing in this account. Both engi- [fol. 118] neers worked with approximately the same inventory of property items, and it is apparent all property has been included by both, in some classification.

The classification of accounts, by account number and description, is shown by the following tabulation.

| Acct. No. | Description. |
|---|---|
| 1301..... | Organization. |
| 1307..... | Production—rights of way. |
| 1310..... | Production—field measuring station structures. |
| 1311..... | Production—other structures. |
| 1312..... | Production—gas-well construction. |
| 1313..... | Production—gas-well equipment. |
| 1314..... | Production—field-line equipment. |
| 1315..... | Production—field measuring-station equipment. |
| 1316..... | Production—drilling and cleaning equipment. |
| 1317..... | Production—other equipment. |
| 1325..... | Transmission—land. |
| 1327..... | Transmission—rights of way. |
| 1328..... | Transmission—compressing station structures. |
| 1329..... | Transmission—measuring station structures. |
| 1330..... | Transmission—other structures. |
| 1331..... | Transmission—compressing station equipment. |
| 1332..... | Transmission—measuring station equipment. |
| 1333..... | Transmission—line equipment. |
| 1334..... | Transmission—other equipment. |

| Acct. No. | Description. |
|---|---|
| 1376 | General—other land. |
| 1379 | General—other structures. |
| 1380 | General—office equipment. |
| 1381 | General—store equipment. |
| 1382 | General—shop equipment. |
| 1383 | General—stable equipment. |
| 1384 | General—garage equipment. |
| 1385 | General—laboratory equipment. |
| 1386 | General—telephone and telegraph system. |
| 1387 | General—tools and implements. |
| 1388 | General—other equipment. |
| 1390 | Engineering and superintendence. |
| 1391 | Law expenditures during construction. |
| 1993 | Taxes during construction. |
| 1394 | Interest during construction. |
| 1395 | Miscellaneous construction expenditures. |
| | Cost of financing. |
| | Working capital. |
| | Material and supplies. |
| | Going concern value. |

The valuation of nine of these accounts is not disputed by the engineers, and the Commission, therefore, adopts their value as follows:

| Acct. No. | | Repro. cost, new. | Repro. cost, new, less dep'n. |
|---|---|---|---|
| 1316 | Production—drilling and cleaning equipment | $32,833 | $27,908 |
| 1376 | General—other land | 3,655 | 3,655 |
| 1380 | General—office equipment | 117,817 | 106,035 |
| 1381 | General—store equipment | 2,123 | 1,805 |
| 1382 | General—shop equipment | 26,991 | 23,084 |
| 1383 | General—stable equipment | 640 | 568 |
| 1385 | General—laboratory equipment | 8,369 | 8,202 |
| 1387 | General—tools and implements | 51,358 | 44,979 |
| 1388 | General—other equipment | 23,877 | 21,832 |

[fol. 119] The remainder of these accounts will be discussed under the order in which they appear in the classification, with the exception of Account 1301, which will be discussed under the heading Intangible Items which follows the discussion of Tangible Items.

## Account No. 1307

## Production—Rights of Way

This account includes rights of way on production field lines, as distinguished from transmission lines, valued by Mr. Black at $33,990. This right of way is valued at $0.85 per rod.

Mr. Hamilton does not show any rights of way under this classification, but he may have included this under Account

No. 1327, Transmission—rights of way. A comparison of exhibits 41A, B and C, and exhibits 17A and B, shows that Mr. Black has allowed a total of 1,212,251 rods for rights of way in Accounts 1307 and 1327, as compared to Mr. Hamilton's allowance of 1,180,102 rods in Account 1327. In other words, Mr. Black has allowed an excess over Mr. Hamilton of 32,149 rods of rights of way.

It is our opinion that an allowance under this account is proper. We find that the fair average value per rod of pipe-line right of way in this system is $1.40, which applied to the 39,987 rods of right of way allocated by Mr. Black to this account, gives $55,982 as the fair value of this account. The development of this average unit price of $1.40 per rod for production rights of way is discussed under Account 1327, Transmission—rights of way.

## Account No. 1310

## Production—Field-Measuring Station Structures

This account includes the buildings and appurtenant constructions housing meters, regulators, and other field measuring equipment, as distinguished from similar structures housing equipment measuring gas delivered by transmission system lines to city gates or other users. These structures are valued by Mr. Black at $40,517, cost of reproduction new, and $35,909 depreciated. Generally the structures covered by this account are sheet metal on wood frames with no foundations and dirt floor. They range from 3 x 5 x 3 feet to 10 x 12 x 8 feet in size, the average size approximating 6 x 8 x 7 feet. Mr. Black's valuation lists 597 of these structures, 43 of which are carried as one item. The average cost per structure is $68 new, and $60 depreciated. Mr. Black testified (Tr. 1777) that in pricing these structures [fol. 120] they were separated into classes by size and type of construction, detailed estimate of materials and costs were worked out for each class, and then the cost applied on a cubic-foot basis.

These structures are valued by Mr. Hamilton at $42,244 new, and $37,194 depreciated. Mr. Hamilton furnished no detail of value of individual structures.

The company introduced exhibit 54 (Tr. 2045), showing in part alleged omissions from Mr. Black's valuation, of twelve meter settings and housings which should properly

be classified under Accounts 1310 and 1315. No separation was made as between these accounts, and the amounts claimed by the company are added in Account 1315.

In pricing these structures, Mr. Black separated them into classes, by size and type of construction, and worked out a detailed estimate of materials and costs for each class in arriving at his cubic-foot basis, and he sets up individual structures in this account on approximately 120 pages of exhibits 41-A, B and C. Mr. Hamilton sets out the value of this account in a lump sum without any detail and without even setting out the number of structures and valuation. He claims to have arrived at his cubic-foot basis upon the experience of many years, but does not give the Commission any data which may have been accumulated by reason of this experience.

Mr. Black and Mr. Hamilton arrived at approximately the same per cent condition for the items in this account. Mr. Black found the cost new, less depreciation, to be $35,909. Mr. Hamilton found the cost new, less depreciation, to be $37,194, or a difference of $1,285.

Mr. Black and Mr. Hamilton, in arriving at the present value of this account, have done so by inspection of the property.

Counsel for the Commission suggest that—

"Inasmuch as this property is dependent upon the life of the gas fields in which it is used, the per cent condition of this account should be based upon the proportion which the recoverable gas in the fields bears to the total of the reserves estimated originally in these fields."

Their basis of arriving at the depreciated value by the depletion method is set out for the purpose of discussion as follows:

"After eliminating storage fields, and making allowance for salvage, we have made a calculation of the present fair value of the property in this account on this basis, excepting in the state of Texas, where it appears from the evidence that the life of the field will equal or exceed that of the property in this account.

[fol. 121] "The development of the present fair value of Account 1310 by depreciating in ratio with depletion of gas fields in Kansas (exclusive of Augusta and Craig fields), Missouri and Oklahoma, and by inspection methods

in Texas, and Augusta and Craig fields in Kansas, is computed as follows:

"Mr. Eastman's exhibit 39 sets out the estimated salvage for Accounts 1310 and 1315 combined, which includes both structures and equipment. In Kansas the estimated salvage of these two accounts (exclusive of Augusta and Craig fields) is $18,275, and the reproduction cost new is $234,303. The estimated salvage is computed as 7.8 per cent of the reproduction cost new. In Missouri the reproduction cost new is $3,997, and the estimated salvage is $500, being 12.5 per cent of the reproduction cost new. In Oklahoma the reproduction cost new is $128,433 and the estimated salvage is $10,415, which is 8.11 per cent of the reproduction cost new.

"Mr. Davis' exhibit 3, pages 60 and 61, sets out the ultimate gas reserves and the reserves as of July 1, 1931, in M cubic feet. In Kansas (exclusive of Augusta and Craig fields) the ultimate reserves are 39,207,458 M cubic feet, and the reserves as of July 1, 1931, are 8,222,000 M cubic feet, which is 20.97 per cent of the ultimate reserves, or a weighted average per cent condition of the fields in Kansas (exclusive of Augusta and Craig fields).

"In Missouri the ultimate reserves are given as 46,648 M cubic feet, and the reserves as of July 1, 1931, as 25,000 M cubic feet. Dividing 25,000 by 46,648, the weighed average per cent condition of the Missouri fields is found to be 53.59. In Oklahoma the ultimate reserves are given as 65,001,665 M cubic feet, and the reserves as of July 1, 1931, as 14,633,000 M cubic feet. Dividing 14,633,000 by 65,001,665 the weighted average per cent condition of the Oklahoma fields is found to be 22.51.

"Taking the adopted reproduction cost new on Kansas (exclusive of Augusta and Craig fields) of $18,839, and deducting 7.8 per cent as computed from Eastman's exhibit 39, as salvage, we find the reproduction cost new, less estimated salvage, to be $17,370. To this figure of $17,370, we apply the per cent condition of 20.97, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage of $3,642, to which the estimated salvage of $1,469 is added, giving a present fair value for Kansas (exclusive of Augusta and Craig fields) of $5,111. In the Augusta and Craig fields we have used Black's depreciated value of $4,598 arrived at by inspection. In Missouri we have taken

the adopted reproduction cost new of $280 and deducted 12.5 per cent salvage, computed from Eastman's exhibit 39, and find that the reproduction cost new, less salvage, is $245. To this figure of $245, we apply the per cent condition of 53,59, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage, of $131, to which the estimated salvage of $35 is added, giving a present fair value for Missouri of $166.

"In Oklahoma we have taken the adopted reproduction cost new of $10,332 and deducted 8.11 per cent salvage, computed from Eastman's exhibit 39, and find that the [fol. 122] reproduction cost new, less salvage, is $9,494. To this figure of $9,494 we apply the per cent condition of 22.51, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage, of $2,137, to which the estimated salvage of $838 is added, giving a present fair value for Oklahoma of $2,975.

"In Texas we have adopted Black's depreciated value of $5,721, arrived at by inspection.

"Adding together the present fair values found for each of the several states, the present fair value for Account 1310 is $18,571 if the present fair value is computed by this method."

This theory does appear to us to be a fair and reasonable basis for determining the present fair value of the property, inasmuch as the property is dependent upon the life of the gas fields in which it is used, and the value of the equipment is returned to the company by amortization and depletion allowance upon such basis. We do not believe, however, that the proper result can be reached by taking the property of the company in the states as a whole and using only the reserves which the company owns for the purpose of this calculation. We are unable to find in the record sufficient evidence upon which to allocate the property to each particular gas reserve, and, therefore, decline to apply this theory of depreciation to the pipe-line property. We might add in passing that if it were possible from the evidence to use this method of depreciation that it would also apply to Accounts 1311, 1312, 1313, 1314, 1315 and 1317, decreasing the present value of the property approximately two million dollars.

We find the cost of reproduction new to be $40,517 and the value of Account 1310 to be $35,909.

## Account No. 1311

### Production—Other Structures

This account is valued by Mr. Black at $59,087 new and $47,876 depreciated. The account covers sixty-six warehouses, dwellings and miscellaneous structures and includes fences, sidewalks and other improvements.

In Hamilton's appraisal this account is valued at $60,832 new, and $50,162 depreciated, and covers the same number of structures as shown by Black. Mr. Eastman testified with respect to this account (Tr. 1108, 1114-1122) that he arrived at a 16c per cubic foot value for the structures based on his general experience. We find the present cost of reproduction new to be $59,087 and the present fair value of this account to be $47,876.

[fol. 123] Account No. 1312

### Production—Gas-well Construction

This account is valued by Mr. Black at $1,718,813 new, and $1,210,392 depreciated. This account covers all costs of drilling gas wells, and the placing in the wells of all casing, tubing and equipment furnished by the owner. The number of wells, location, and the items entering into their construction was taken by Black from an inventory furnished by the company.

Mr. Black's development of unit cost is illustrated by his testimony with respect to Fuqua Well No. 2. He testified that the allowance for items in this account was broken down into a unit price per foot for the contract drilling on gas wells; and that in addition allowances had been made for day work, for fuel, for water, for depreciation of casing withdrawn and used, for transportation of casing and tubing and for superintendence during the drilling period. A. S. Ritchie also testified with respect to drilling costs estimated by him on Fuqua No. 2 and Burnett No. 14.

A comparison of Mr. Black's, Mr. Hamilton's and Mr. Ritchie's valuations of certain wells, completely equipped is found on transcript page 2891, and follows herewith:

| | | | Ritchie | |
|---|---|---|---|---|
| Well | Black | Hamilton | Standard rig | Rotary |
| Fuqua No. 2 | $19,843 | $24,991 | $22,303 | $22,101 |
| Burnett No. 14 | 30,024 | 32,847 | 27,301 | 23,779 |

The property in this account is valued by Mr. Hamilton at $2,022,296 new, and $1,300,025 depreciated.

In support of the cost of reproduction new used in Hamilton's appraisal, the gas company introduced, as exhibits 65 to 70, inclusive, photographs of job orders and vouchers covering Fish No. 2, Charty No. 2, Freyler No. 1 and No. 2, and Fuqua No. 2. Mr. Eastman's development of unit costs per foot of drilling was developed from the company's experience in drilling in these various fields, and no testimony covering the details of the development other than the actual cost to the company for the drilling of these wells originally was ever introduced by Mr. Eastman or Mr. Hamilton. Original costs were introduced, letters from other gas companies covering cost of wells drilled in approximately the same territory were introduced, but at no time was any breakdown of the figures used by Mr. Hamilton in his exhibit 41A ever given in response to examination of the company's witnesses.

In addition to the matters above mentioned reflecting on [fol. 124] the value to be allowed for this account, our judgment is influenced by another consideration. Mr. Ritchie, production manager for the Derby Oil Company and theretofore production and pipe-line superintendent of the Marland Oil Company, having had fourteen years experience in drilling and contracting wells in Kansas, Oklahoma, Texas, New Mexico and California, testified that he was familiar with costs of drilling wells in the Amarillo Proven Sweet Gas Fields in September, 1931; that by use of rotary tools, wells could be drilled in this field at this time at a less cost than if standard tools were used, and that the Fuqua well No. 2 and the Burnett well No. 14, concerning which respondents introduced testimony as to their actual cost, could be completed at what is known as turnkey job prices as follows: The Fuqua well No. 2 at $22,303 with standard and $22,101 with rotary tools; and that the Burnett well No. 14 could be completed for $27,301 with standard and $23,770 with rotary tools. Mr. Black's complete costs on these two wells are as follows: Fuqua well, $19,843 and Burnet well No. 14, $30,024, and total considerably more than it would actually cost to complete these wells, as testified to by Mr. Ritchie. We are of the opinion that Mr.

Ritchie is a man of wide experience in this kind of work. He testified that the estimate of cost of these wells as given by him were estimates on which he would be willing to contract to complete the wells and we believe they are accurate. In addition he stated that if he had twenty wells to drill his cost would be reduced five per cent. The evidence here shows that in the Amarillo field respondents have sixty wells and it is fair to presume that in the case of a contractor taking a contract to drill sixty wells, a deduction of more than five per cent might be made. We think it is fair to use the figures given by Mr. Black as the reproduction value of these wells, inasmuch as they are higher than those given by Mr. Ritchie, and this applies to the total valuation as found by Mr. Black. Mr. Black found a cost of reproduction new for this account in the amount of $1,718,813. This account includes storage wells in the Craig and Augusta fields. The reproduction cost new given these storage wells by Mr. Black, totaled $130,363. It is our opinion that the value given these wells should be deducted from this account. A storage well is one which was formerly drilled for gas and has been abandoned for that purpose after the gas is depleted. The record shows that the respondents have two fields which they use for storage, one known as the Craig field and the other as the Augusta field. These fields are used as a reservoir into which gas is placed [fol. 125] during the summer months when the demand for gas is low, as a reserve to be used when the demand is greater. The record shows that the company, after the gas in those particular fields was exhausted, entered into contracts with the land owners whereby they leased these lands and these abandoned wells for storage purposes. We believe that these abandoned wells (referring only to the hole) belong to the landowners and not to the company and that they are simply leased to the company for the purposes mentioned in the storage contract, and that the company has no title to them and they should not be included in the valuation of respondents' property. We have, therefore, decreased Mr. Black's reproduction new value for this account of $1,718,813 by $130,363, or to $1,588,450. We find the present fair value of this account to be $1,153,157.

## Account No. 1313

### Production—Gas-well Equipment

This account covers all casing, tubing and fittings in the wells. The account is valued by Mr. Black at $658,245 new and $484,514 depreciated. The inventory of these items was furnished by the company and unit prices were applied developed by Black.

Mr. Hamilton values this account at $917,777 cost of reproduction new, and $573,124 cost of reproduction depreciated.

The testimony with respect to the allowances for casing and tubing included in this account is apparently conclusive with respect to the prices fixed by Black being insufficient, while the testimony is not conclusive that the prices used by Mr. Hamilton were representative prices as of the date of his valuation. However, we have accepted his total of $653,309 for casing and tubing in this account, corrected for overheads which we believe to be excessive, and have applied instead the overheads used by Mr. Black. The net difference in the allowance for casing and tubing at the site of the wells between Mr. Hamilton's and Mr. Black's valuations is $288,617, including overhead.

The testimony with respect to allowances for casing and tubing included in this account was emphatic with respect to the purchase of such materials from local supply houses because of the necessity of immediate delivery when the need for such supplies developed. However, the overhead allowances included by Mr. Hamilton were made up of two items, 5 per cent for warehousing and an additional 5 per cent calculated on the price of casing and tubing plus ware- [fol. 126] housing, for omissions and contingencies, or a total of 10.25 per cent on the price of these materials. Mr. Black allowed in his exhibit 42, "Unit Cost Analysis," a total of 3½ per cent structural overheads on pipe and casing made up by an allowance for omissions and contingencies of ½ per cent, 1 per cent for purchasing, ½ per cent for supervision and inspection. These allowances we find to be proper and ample. We have, therefore, corrected this account by using Mr. Hamilton's prices for casing and tubing to which we have applied Mr. Black's overhead percentages, giving a cost of reproduction new of $894,618 for this

account. Applying the per cent condition used by Mr. Black of 73.6 per cent, we find a cost new, less depreciation, of $658,439.

## Account No. 1314

## Production—Field-line Equipment

This account covers the labor and materials necessary to construct and test pipe lines between the wells and the transmission system. The account is valued by Mr. Black at $3,548,102 new, and $3,126,159 depreciated. Items in this inventory were taken from the pipe-line maps of the company. Prices of pipe, materials and labor developed by Mr. Black have been used in arriving at the total of this account. In Texas, gathering lines up to and including four-inch were priced on the basis of being buried at half the depth of main line. In other states gathering lines up to and including 12¾-inch were considered as being placed in trenches half the depth of main line of the same size. Mr. Black testified that this assumption was fair and that throughout the system there were 747,000 feet of gathering lines and 230,000 feet of transmission system mains above ground, but that the lack of time had prevented the accurate location of such lines, and they were all considered as being in trench and were so priced.

Mr. Hamilton values this account at $4,447,806 reproduction cost new and $4,169,763 depreciated. From an examination of Mr. Hamilton's exhibit it appears that there is a difference of opinion concerning lines falling in Account 1314, Producton—Field Line Equipment, and Account 1333, Transmission Line Equipment. Mr. Black may have included in one account what Mr. Hamilton may have included in another, but the lines allocated to both accounts comprise the entire system of field and transmission lines.

Consideration of this Account 1314 involves an analysis of cost of pipe, excavating and back-filling, pipe laying and [fol. 127] all other elements of cost appearing in Account 1333. Each of the items involved covers considerable space in the record, and the situation is simplified by considering the items common to both accounts and making such modifications as appear proper at one time, and these matters will be discussed later. We choose to follow counsel's suggestion and to consider any adjustment in pipe prices under

Account 1333. Respondents question counsel's attempted corrections of pipe prices in this account of page 28 of their reply brief, stating that they will discuss the matter when they reach Account 1333. We are, however, unable to find any assistance in adjusting pipe prices from further discussion in respondent's reply brief. We find the reasonable value of this account to be $3,548,102 new, and the present value of this account to be $3,126,159.

Account No. 1315

Production—Field Measuring-station Equipment

This account is valued by Mr. Black at $298,526 new and $261,887 depreciated. This account covers all measuring equipment, valves, pipes and fittings, not a part of production field line equipment, for measuring of gas in the field.

Mr. Hamilton values this account at $402,535 new, and $385,746 depreciated. There is no detail of this account in Mr. Hamilton's exhibits other than total costs of reproduction by fields, excepting where the number and unit prices of meters are indicated; there is, therefore, no way to check the number of installations covered by Mr. Hamilton's exhibit. The company introduced exhibit 54 (Tr. 2045) and called Mr. Black's attention to the alleged omission of fifty-one stations from Mr. Black's inventory, which was detailed so individual stations could be checked against it. These stations were never identified by Mr. Black and there is no testimony showing that they were included or excluded in this account, or that they were in fact in existence at the time of his inspection. The gas company's inventory, as stated before, shows no detail with respect to these stations, so exhibit 54 cannot be checked against Mr. Hamilton's exhibit.

The company claimed that these fifty-one stations total $27,865 new, and in order to eliminate any argument concerning whether they have or have not been included in Mr. Black's valuation, we are adding $27,865 to his reproduction cost new in Accounts 1315 and 1332. Exhibit 54 does not separate these stations between Accounts 1310 and 1315, 1329 and 1332.

[fol. 128] We have added to Mr. Black's reproduction new, of $298,526 for this account, $4,085.00 claimed by the company for the twelve stations omitted from Accounts

1310 and 1315, and find a cost of reproduction new for this Account 1315, of $302,611. We have added to Mr. Black's present fair value of this account of $261,887, the company's depreciated value for these stations of $3,859, making a total of $265,746, which we find to be the present fair value of this account.

Account No. 1317

Production—Other Equipment

This account consists of water tanks, water wells and one windmill used in connection with the company's production operations. It is valued by Mr. Black at $1,501 new, and $1,206 depreciated.

Mr. Hamilton valued this account at $1,774 new, and $1,461 depreciated.

On consideration of this account and the fact that there is little difference between the valuations of Mr. Hamilton and Mr. Black and the evidence on the valuation, which is not detailed and no unit values given, we find that the fair value of this property is $1,637 new, and $1,333 depreciated.

Account No. 1325

Transmission—Land

This account is valued by Mr. Black at $149,202, and is undepreciated. The company appraised all real estate for the purpose of this valuation and furnished the above total to Mr. Black, and it was adopted by him without check. This land in general is occupied by compressing stations, meter stations and other miscellaneous structures required in the operation of the transmission system. It comprises all land owned in fee by the company with the exception of Account 1376, General—Other Lands, which includes a telephone office site at Douglass, Kan., warehouse sites at Caney, El Dorado, Emporia, Petrolia and Tyro, Kan., and a meter shop location at Bartlesville, Okla.

The testimony in this case is conclusive to the effect that the Hominy, Owasso and Hogshooter compressing stations have not been used for several years and are not now used or useful in the operation of this system. We have there-

fore deducted $4,000 for compressing station sites at Owasso and Hogshooter, and find the present fair value for this account of $145,202.

[fol. 129] Account No. 1327

Transmission—Rights of Way

This account covers both pipe-line and telephone-line rights of way. It is valued at $1,174,574, and is not depreciated.

Mr. Black allowed in Accounts 1307 and 1327 for 1,212,251 rods over Mr. Hamilton's allowance of 1,180,102 rods. Mr. Black also allowed in Account 1327 for 65,440 rods of telephone-line rights of way, an excess of 50 rods over Mr. Hamilton's allowance of 65,390. Mr. Black allowed 85 cents per rod for pipe-line rights of way on pipe lines under 16-inch, and $1.20 per rod for pipe-line rights of way for lines over 16-inch, and 25 cents per rod for telephone-line rights of way. His prices were predicated (Tr. 2164) on studies of right of way cost data in Texas, Oklahoma, Kansas and Missouri, and were based both on cost of rights of way (Tr. 2164) in Oklahoma and Kansas, and on valuation costs of the Lone Star Gas Company in Texas and Oklahoma; the Oklahoma Natural Gas Company in Oklahoma; the Oklahoma Power and Water Company valuation in Oklahoma; the Panhandle Eastern and the Panhandle Illinois Pipe-Line Company in Kansas and Missouri. Mr. Black's breakdown of unit cost allowance for rights of way (Tr. 2167) allowed the following items and amounts:

Cost of right of way, 50 cents per rod.

Damages and fencing for lines under 16-inch, 20 cents.

Damages and fencing for lines 16-inch and over, 45 cents.

Cost of securing right of way for lines under 16-inch, 15 cents.

Cost of securing right of way for 16-inch and over, 24 cents.

Mr. Black's allowances also included all items of expense involved in the securing and recording of deeds and making the necessary transactions. It also included abstracting and notary's fees. These figures are developed (Tr. 2168) as follows:

| | |
|---|---|
| Cost of securing right of way, 88 men working over a four-month period at $500 per month | $176,000 |
| Allowance for transportation | 4,000 |
| Legal expenses | 12,000 |
| Miscellaneous expenses | 10,000 |
| Total | $202,000 |

Mr. Black considered that there would be in round numbers 3,000 miles of right of way, which divided into $202,000 gives a figure of 21 cents per rod for cost of securing rights of way. He allowed a cost, therefore of 15 cents per rod for securing rights of way on the smaller lines and 25 cents on the larger lines. Mr. Black's average allowance [fol. 130] per rod for pipe-line rights of way in Accounts 1307 and 1327 is $1,208,564 divided by 1,212,251 rods, $0.997 per rod.

Mr. Montgomery (Tr. 2768) introduced exhibit 87 showing the cost to the company of rights of way acquired on some twenty pipe lines. This exhibit covers a total of 6,215,512 feet of line; the right of way and damage costs totaled $407,179.82, or an average cost of $1.08 per rod. The rods of right of way covered in Montgomery's exhibit total 376,698, or 31 per cent of the total of 1,212,251 rods of right of way in Accounts 1307 and 1327. Of the total rods of right of way covered by Mr. Montgomery's exhibit 87, 171,638 rods are for lines under 16-inch and 205,060 rods for lines 16-inch and over. Applying Mr. Black's allowances of 85 cents per rod and $1.20 per rod, his allowance for the right of way in this exhibit is $391,964, or $15,216 less than cost of right of way and damages of $407,179.82, shown by Mr. Montgomery's exhibit 87. The right of way secured for the lines covered by this exhibit 87 covered the period from April, 1928, to October, 1931, and costs thereof were probably in excess of those obtaining at the time of this inquiry, due to decreased values.

Respondents contend that Mr. Montgomery's figures were obtained from analysis of job orders which do not contain all of the items of cost such as legal work in connection with securing rights of way, notary fees, et cetera.

An allocation of all the expense of the pipe-line company entering into these accounts indicates that the addition, because of these items, would add very little to the rights of way cost.

Mr. Hamilton's value on this account is $3,696,804. Mr. Hamilton's value per rod for pipe-line right of way averaged $3.25 per rod in Kansas, $3.27 per rod in Missouri, $3.27 per rod in Nebraska, $3.12 per rod in Oklahoma and $2.11 per rod in Texas. Transmission rights of way on the lines of the Cities Service Gas Pipe Line Company in Kansas averaged $2.43 per rod, and in Oklahoma and Texas $2.11 per rod. Mr. Hamilton's exhibit includes pipe-line rights of way of the American Pipe Line Company in Kansas and Missouri, $3.45 per rod. Mr. Eastman testified that in the figures quoted above, all costs incident to obtaining the right of way and in preparing it up to the point when the pipe line is laid, together with all settlement for damage claims arising from the laying of the lines, were included, and on transcript page 1286 he named the following items: Aerial surveys, 10 cents per rod; field survey in staking the route of a line, 19 cents per rod; right of way payments for purchase or easements from landowners, [fol. 131] $1.25 per rod; crop damages, damages to fences and trees, 70 cents per rod; expense of obtaining right-of-way agreements; 30 cents per rod; abstracting and recording of rights-of-way agreements, 10 cents per rod; miscellaneous expense, 10 cents per rod; clearing, grading and fences, 80 cents per rod, making a total of $3.54 per rod.

Lower costs were testified to by Mr. Eastman in Cowley county, Kansas, where a cost of $2.86 was used; Mr. Eastman testified that these costs were predicated on actual experience of the Cities Service Gas Company and other pipe-line companies of which he has knowledge, including the Continental Construction Company pipe line from the Texas fields to Joliet, Ill., and on transcript, page 1290 he testified that his costs were based primarily on the experience of the Continental Construction Company and on the experience of the Cities Service Gas Company on certain lines that have been recently laid, but he furnished no data as to the experience of any of these companies.

The company introduced two other witnesses who testified on the cost of right of way. J. S. Gibson, right-of-way agent for the Prairie Pipe Line Company, testified to nothing specific excepting that he considered the allowance by Mr. Black to be too low.

We do not believe that the allowance made by Mr. Hamilton for aerial survey is proper. The line was constructed

with the advantage of an aerial survey. As this line has been constructed without an aerial survey it would be improper to allow the cost of an aerial survey and in addition the increased costs in the valuation due to the fact that an aerial survey has not been made, and would not be used in reproducing the company's pipe line along a route already determined.

If the present cost of reproducing the pipe line is greater because in laying it over it did not have the advantage of an aerial survey it would certainly be improper to allow the additional cost of an aerial survey.

Mr. Hamilton also makes an allowance for grading and fencing. Mr. Black has made this allowance under his construction cost. From the testimony of the witnesses we believe this to be the proper place to handle this item.

Mr. Hamilton makes an allowance for legal expense under legal expense during construction. He testified that, "That would include all of the legal expenditures for the incorporation, and for the drawing of contracts, for all of the type of work that must be done prior and during the con- [fol. 132] struction of the property." (Tr. 1541.) It would therefore be improper to include legal expense in the cost of obtaining rights of way. Mr. Montgomery submitted exhibit 87, showing the actual cost of acquiring rights of way, to the company, on over 31 per cent of the line in controversy, to be $1.08. The company's contention is that the exhibit prepared by Mr. Montgomery from the company's job orders does not include all the costs of acquisition of the rights of way, such as going out and securing right of way, securing abstracts and recording them, including the expense of the men in the field, the automobile expense, telephone calls, legal expense and locating rights of way.

Mr. Black's average cost per rod of the whole system is 99 cents. This figure is 9 cents below the actual cost to the company, as reflected by the job orders. This cost of $1.08 occurred during the years 1928, 1929, 1930 and 1931. This must be recognized as a period of high prices and expensive pipe-line construction, and it is reasonable to assume that the prices at that time were influenced upward by those existing conditions.

Mr. Black has included engineering and staking out under the engineering account, No. 1390. The cost of clearing,

grading and construction damages have been included under construction cost. These items appear to be properly included in these accounts under the practice of the company. Exhibit 38 consists of one of the construction contracts under which the contractor agrees to perform the following services: Clearing the right of way before construction and cleaning up right of way after the completion of the work, to make all repairs to fences, and all cost of other improvement damages.

"Such damages for which the contractor is responsible includes repairs to fences, hedges and roads, and damage done to or by stock escaping through fences or gates left open or insecurely closed, as well as any and all damages to stock on account of being frightened, damage due to cutting hedges, damages to travelers in horse-drawn or automotive equipment, or stock, caused by open ditches, and in general any damages that might have been avoided by care on the part of the contractor. All such claims for damages for which the contractor is liable shall be settled by the contractor." (Ex. 38.)

This contract also provides that the contractor is to receive construction material furnished by the company at rail points closest the work and to transport such material used in excavation and construction of the pipe line and back fill for certain stipulated prices. Grading of the rights of way, which is a construction cost, is not mentioned in the [fol. 133] items which the company is to furnish or perform for the contractor, and is included as an item incidental to excavation.

In view of Mr. Montgomery's analysis of rights-of-way costs, we are of the opinion that Mr. Black's allowances should be increased to an average over the entire system of $1.40 per rod to cover all costs of acquisition, damages and other incidental costs chargeable directly to right-of-way cost. We have, therefore, allowed for Account 1307, Production—Right of way, 39,987 rods at this average price of $1.40 and have carried this total for Account 1307 as $55,982. We believe the total fair value for pipe-line right of way in Account 1327 to be $1,641,170, and for telephone rights of way to be $16,360, or a total for Account 1327 of $1,657,530. In arriving at this figure we have applied an average price of $1.40 per rod to 1,172,264 rods of pipe-line

right of way and a price of 25 cents per rod to 65,440 rods of telephone line.

We have arrived at the figure of $1.40 per rod by taking the actual average cost of right of way and damages of $1.08, as shown by the books of the company, and have added thereto 22 cents per rod for expense of acquisition and 10 cents per rod for the expense of abstracting and recording, which is the average cost of these items as testified to by Mr. Hicks, the right-of-way agent for the company.

We find the present fair value of Account 1327 to be $1,657,530.

## Account No. 1328

### Transmission—Compressor-station Structures

This account includes all structures and appurtenant construction for compressing station operation, including dwellings, garages, machine shops, dams and buildings housing compressors.

The account is valued by Mr. Black at $1,806,823 new and $1,567,605 depreciated. In pricing these structures Mr. Black had available detailed drawings on important structures, and also such information as was contained in the company's exhibit 17. Inspection was made in the fields of all structures in this account, sizes were checked, bills of material were prepared, and the prices applied were carefully developed for all structures of a given type; on patented buildings, much of the data with respect to cost were developed directly from the manufacturer.

This account is valued by Mr. Hamilton at $2,482,629 new and $2,267,443 depreciated.

There is no detail in Mr. Hamilton's valuation of the cost [fol. 134] of major items such as buildings, the unit cost appearing in each case being a total for a building. For example, on page 116 of his exhibit 17B, the first item at the top of the page is the main compressor building at the Wichita station. The building is described as being 69′ 6″ x 229′ 3″ x 35′ 0″; foundation, concrete and bricks; walls and roofs, corrugated steel; floors, concrete; unit cost, $72,494.63.

The testimony of Mr. Eastman in support of these lump-sum costs was that they had been arrived at by applying a

cubic-foot unit price to the volume of the building and that such unit costs had been developed through the company's experience in construction, and that no further breakdown was possible excepting to separate superstructures and foundations. Contrasted with such testimony, Mr. Black testified in minute detail concerning his development of labor, materials, and overhead costs and his method of applying them to items of material entering into the construction of such structures.

W. D. Truman, construction engineer for the Kansas City Structural Steel Company, and George P. Reintjes, a contractor of Kansas City, testified on behalf of the company. Mr. Truman made estimates of cost of the main structures at five compressing stations, by using estimates prepared by Mr. Reintjes on the foundations of these structures, and adding superstructure costs developed by himself. His estimates covered roughly 32 per cent of the total cost of these structures as estimated, and Mr. Reintjes estimated approximately 68 per cent of the total. Mr. Truman testified (Tr. 2336-2341) that he estimated the cost of the main compressing station buildings of the company at Higgins, Tallant, Drumright, Ottawa and Grabham. That he estimated superstructures only, and that all excavation and concrete foundations, electric lighting and other construction was estimated by George P. Reintjes, of Kansas City, and the figures furnished him were added to his estimates of superstructures in order to get the total for each structure. Mr. Truman compared these estimates with the values found for the same structures by Mr. Black. That comparison follows

| Station. | Black's valuation. | Truman's valuation. |
|---|---|---|
| Higgins | $38,010.00 | $64,115.00 |
| Tallant | 26,953.00 | 43,885.56 |
| Drumright | 23,610.00 | 46,679.98 |
| Ottawa | 40,232.00 | 52,677.49 |
| Grabham | 51,601.00 | 77,197.00 |

[fol. 135] Mr. Reintjes testified (Tr. 2350) that he estimated the foundations, gave his figures to Mr. Truman, and that by subtracting his figures Mr. Truman's superstructures allowances could be determined. This operation is shown by the following table:

| Station | Truman's valuation, including Reintjes' estimates | Reintjes' estimate of foundations, etc. | Truman's valuation of superstructures |
|---|---|---|---|
| Higgins | $64,115.00 | $45,400.00 | $18,715.00 |
| Tallant | 43,885.56 | 29,403.56 | 14,482.00 |
| Drumright | 46,679.98 | 36,313.58 | 10,366.40 |
| Ottawa | 52,677.40 | 34,924.00 | 17,753.40 |
| Grabham | 77,197.00 | 49,410.36 | 27,786.64 |

Mr. Black (Tr. 2473, 2474) compared his valuation of the superstructures with the valuation by Mr. Truman as follows:

| Station | Truman's valuation of superstructure | Black's valuation of superstructure |
|---|---|---|
| Higgins | $18,715.00 | $18,530.11 |
| Tallant | 14,482.00 | 13,020.00 |
| Drumright | 10,366.40 | 10,858.00 |
| Ottawa | 17,753.40 | 17,784.32 |
| Grabham | 27,786.64 | 24,502.00 |
| Total | $89,103.44 | $84,694.47 |

Mr. Black's total was within 5 per cent of Mr. Truman's total on these items.

George Renner, of Topeka, an experienced estimator on building construction, testified (Tr. 2440) that he had checked the plans of the Ottawa and Grabham compressor stations estimated by Mr. Reintjes, and that if bidding on the work at Ottawa his bid would be $28,434, as against $45,019 by Mr. Reintjes. Both estimates have the heating and lighting eliminated, and at Grabham his bid would be $19,048 on the same items Mr. Reintjes estimated at $29,617.

Mr. Black introduced, as exhibit 53, photostats of the sworn returns, dated February 1, 1931, of the company on value for taxing purposes, to the Oklahoma Tax Commission. This report states that as at the date of that return the Hominy compressor station was being reclaimed, and that the Hogshooter compressing station, "is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000." The Owassa station is twenty-five miles or more from any lines of the company; the equipment has been moved and the station is not in use.

Mr. Eastman testified (Tr. 2524) that during the last three or four, possibly five years, the Hogshooter station has not been operated due to the fact that the compressor station capacity was installed at the Tallant station. He [fol. 136] testified (Tr. 2524) that the company was refrain-

ing from using the Hogshooter station because of the necessity of repairing an 18-inch line extending north from that station so it will be capable of carrying high pressure.

In the reply brief counsel for the respondents suggest that the Commission should give no weight to the sworn affidavits before the Oklahoma Tax Commission, stating that these stations were no longer used and useful, because the company may have been over-zealous in its attempt to reduce taxes. We believe that these affidavits, in connection with the other testimony, clearly show that the stations are not at this time used and useful. We condemn he act on the part of the company by which they state, under oath, to one Commission that property is not used and useful for the purpose of defeating their obligations to the government, and make an opposite statement, under oath, to another Commission for the purpose of increasing their revenue at the expense of the general public.

This attempt on the part of the respondents in this case to add approximately a million dollars to the valuation by including compression stations properties in Oklahoma is an illustration of perverted corporate practice. Only a company drunk with power or saturated with arrogance would try to hoodwink a regulatory body in such manner. This Commission does not look with favor on such methods that would bolster a utility valuation in a rate case and at the same time avoid paying its fair share of tax revenue to the states.

In view of these facts we find that these three stations should be eliminated from consideration and we are deducting the value of buildings at these stations from the reproduction new and depreciated values, in arriving at our conclusions.

The company introduced, as exhibit 10, a report of per cent condition of this account as arrived at by inspection by P. McDonald Biddison, a consulting engineer of experience; J. H. Biddison, trained by P. McDonald Biddison; and F. D. Renfro, superintendent of compressor stations of the company. Mr. Eastman (Tr. 1312-1336) compared his own estimates of per cent condition of the property in this account with those of these three other experts, and showed that he had generally used a higher per cent condition than Mr. Biddison; in some cases Mr. Eastman used

a per cent condition 15 per cent higher than Mr. Biddison's, but ordinarily the difference ranged from 1 to 5 per cent.

Mr. Black also determined the per cent condition of the property in this account by inspection and found an average [fol. 137] condition 4½ per cent lower than that of Mr. Eastman's. Mr. Black's per cent condition appears ample in the light of the testimony of the company's experts.

After consideration of all evidence and exhibits, we find the reproduction cost new of this account to be $1,668,151, and the present fair value to be $1,466,102.

### Account No. 1329

### Transmission—Measuring Station Structures

This account includes all measuring structures, housing materials and regulating equipment, including town-border stations. The account is valued by Mr. Black at $147,337 new, and $133,310 depreciated. The account is detailed on pages 943 to 1145, 1731 to 1733 and 1861 to 1863. These structures were checked in the fields for size, were classified with respect to size and type and the price developed on the basis of detailed estimates of qualities for each class of structure, for the approximately 900 structures in the account. The company introduced exhibit 54 (Tr. 2045), showing alleged omissions from Mr. Black's valuation of 39 meter settings and housings, which should be classified under Accounts 1329 and 1332. No separation was made in exhibit 54 of these accounts and the amounts claimed have been added in Acocunt 1332.

Mr. Hamilton's exhibit 17 shows a total value of $165,893 new, and $155,018 depreciated for this account. No details were given as to the number of structures and no testimony was offered by any of the company's witnesses concerning such totals. We find the present fair value of this account to be $133,310.

### Account No. 1330

### Transmission—Other Structures

This account comprises small office buildings, barns, dwellings, storehouses, warehouses, garages and miscellaneous structures and improvements used in connection with the operation of the transmission system. The account is

valued by Mr. Black at $128,764 new, and $113,341 depreciated.

Mr. Hamilton values this account at $131,503 new and $118,604 depreciated.

We find the present fair value of this account to be $113,341.

[fol. 138] Account No. 1331

Transmission—Compressor-Station Equipment

This account covers all machinery and equipment used in connection with the operations of compressor stations. The account is valued by Mr. Black at $9,660,183 new and $8,482,419 depreciated.

A field check was made by Mr. Black of the items in this account from a detailed inventory furnished by the company, and costs of compressors and other equipment was determined by quotations from manufacturers.

Mr. Hamilton valued this account at $9,773,798 new and $8,873,812 depreciated.

Both Mr. Black and Mr. Eastman fixed the per cent condition of the property in this account by inspection. The company introduced exhibit 10 to show the per cent condition observed by P. McDonald Biddison and Mr. Renfro, who also observed the per cent condition of compressing station structures. Mr. Eastman did not use the observed condition per cent fixed by Mr. Biddison and Mr. Renfro, but applied a somewhat higher per cent. He testified (Tr. 1341-1345) to applying 85 per cent condition to main compressor units to which Mr. Biddison and Mr. Renfro applied 80 per cent; he applied 95 per cent condition to auxiliary equipment to which Mr. Biddison and Mr. Renfro applied 85 per cent; he used 85 per cent on machine shop equipment to which Mr. Biddison and Mr. Renfro applied 70 per cent; he applied 85 per cent condition to miscellaneous equipment at Tallant station to which Mr. Biddison and Mr. Renfro applied 75 per cent.

It therefore appears that the fact that Mr. Black's per cent condition on this account is 3 per cent less than that of Mr. Eastman is not out of line when compared with the per cent condition fixed by Biddison and Renfro.

Attention was directed in our discussion of Account 1328, Transmission—Compressing Station Structures, to our conclusions omitting the Owassa, Hominy and Hogshooter stations, because they are neither used nor useful and we have eliminated from this account $705,957, for the reproduction cost new and $433,509 for the present fair value of equipment in these three stations.

We find the reproduction cost new of this account to be $8,954,226 and the present fair value to be $8,048,910.

[fol. 139] Account No. 1332

Transmission—Measuring-Station Equipment

This account includes measuring station equipment, regulators and pipe fittings entering into the installation thereof, dust separators and other miscellaneous equipment used for measuring gas. These items were checked in the field and prices applied in accordance with quotations received from manufacturers in the case of equipment, and developed prices applied to those structural items on which it was necessary to make calculations.

This account is valued by Mr. Hamilton at $1,174,804 new, and $1,143,231 depreciated.

Regulators and meter settings in Kansas are carried in Mr. Hamilton's appraisal at $599,993, without explanation; regulators and meter settings are carried in Missouri at $99,033 and the same item is carried for Oklahoma at $156,487. Testimony in connection with these lump-sum items was given by Mr. Eastman (Tr. 1331) to the effect that meter and regulator statistics were too voluminous to include in detail in his report.

The company introduced exhibit 54 (Tr. 2045), showing 39 meter settings and housings had been omitted by Mr. Black from Accounts 1329 and 1332. Exhibit 54 does not allocate these items between Accounts 1329 and 1332 and so the entire amount is added to Account 1322 in the amount of $25,100 to reproduction new, and $24,006 depreciated.

With the exception of the items listed in Exhibit 54, the company gives no detail of this account. Mr. Black's items were segregated, and in such detail the company was able to detect the omission of thirty-nine stations, the reproduction cost of which was $25,100. Mr. Hamilton arrived at this account in Kansas in a lump sum of $599,993 (Tr. 1351).

In our opinion the totals arrived at by Mr. Black for cost of reproduction new and depreciated are fair when the amounts noted above for thirty-nine stations are added. We find the present fair value of this account to be $759,625.

Account No. 1333

Transmission-Line Equipment

Transmission-line equipment includes the largest item of value in any account. Mr. Hamilton's cost of reproduction new being $46,893,014 and cost of reproduction new less [fol. 140] depreciation $43,578,602, while Mr. Black's cost of reproduction new was $43,099,711, and cost of reproduction new less depreciation $38,842,371.

There were many points of difference between Mr. Black and Mr. Hamilton as to many of the items entering into this account and a great volume of testimony and many exhibits were introduced relating to this account.

As we have said in connection with our discussion of production field line equipment, Account No. 1314, we shall discuss the later account and the transmission-line equipment account together, because both of these accounts include common items of cost of construction, labor and material.

Mr. Black's exhibit 42 consists of 440 pages of the detailed development of direct, overhead and unit prices of pipe and other materials entering into the construction of this property. Pages 1 and 2 of this exhibit is an analysis of the direct structural overhead in Kansas for labor and materials, showing the amounts, in per cent, allowed for omissions and contingencies, purchasing, stores, expense, supervision and inspection, workmen's compensation, public liability, tool expenses, miscellaneous construction expense, performance bond and contractor's profit. Similar analyses are given for Missouri, Oklahoma, Nebraska and Texas.

Page 11 is a development of labor cost for the installation of pipe fittings and valves. Pages 14 to 17, inclusive, develop the cost of pipe of all kinds, delivered for each of the five states in which the gas company has lines. This pipe cost development shows size and kind of pipe, weight per foot, and the cost per foot, including overheads, delivered in Kansas, Oklahoma, Texas, Missouri and Nebraska. On

pages 18 to 25 there is developed labor costs for the unloading, hauling, stringing, ditching and laying of these lines. Pages 24 to 440 develop the cost, installed, of valves, fittings and other items entering into the construction of the system. In the case of general building construction, and in cases where materials or labor prices are not covered by exhibit 42, and where the prices developed in the exhibit required further explanation or breakdown, or where further explanation or breakdown was requested, it was given by Mr. Black in the detail desired.

Contrasted with this exhibit 42 and the testimony of Mr. Black on the development of labor and materials costs is the testimony of Mr. H. L. Eastman, testifying in support of Mr. Hamilton's valuation exhibit, and the unit cost used therein. The only exhibits showing development of unit costs used in Mr. Hamilton's exhibits were introduced by [fol. 141] Mr. Black as exhibits 73 and 74, covering data received by Br. Black from Mr. Eastman.

Mr. Eastman, testifying on the breakdown of labor prices used in Mr. Hamilton's exhibit for unloading, hauling, stringing, ditching, laying pipe and backfilling the ditch, said he had no breakdown of such prices, or of the supporting data back of them, other than analyses his company had made of actual construction costs during the period dating back to 1924. He was in all cases unable to testify concerning the data underlying the figures used, excepting that it was too voluminous to produce in court. His testimony with respect to development of "pick rock" and "shoot rock" prices was the same. This underlying data was developed according to Mr. Eastman by putting men out on construction jobs and analyzing the contractor's costs of each operation.

The contract cost for pipe-line construction, as shown by the construction contracts under which much of the pipe-line system of these companies has been constructed, is usually on the basis of one unit price per foot for unloading the pipe, hauling, stringing, ditching, in all classes of excavation, laying the pipe and backfilling. It is apparent that when such construction operations are analyzed in accordance with Mr. Eastman's testimony, and the costs so developed are applied to units of work done, and the total so arrived at is compared with the contract cost by a reputable contractor for the same operations, there should

be some reasonable relation between the two, but the record in this case does not indicate any such relation. Mr. Black's exhibit 77 compares the contract costs of unloading pipe and materials, hauling, stringing, ditching in all classes of materials, laying pipe, backfilling and testing on seven of the lines in this property with the amounts claimed in Mr. Hamilton's exhibit for "pick rock" and "shoot rock" only. Line "G" between Wichita and Ottawa, cost the company $0.59 per foot for all the above operations, including rock excavation, under a contract dated June 22, 1928, or a total of $379,699. Mr. Hamilton's valuation, based on an analysis of costs of contract operations, shows the cost of rock excavation only to be $390,276, or $10,577 more than the contract cost of all operations for the construction of this line excepting welding and painting. Mr. Eastman testified that Mr. Hamilton's classification of earth, shoot rock and pick rock in the pipe lines of the system was determined by engineers sent over the lines for that purpose. Mr. Eastman testified that where any shoot rock was shown in the valuation it had been calculated as solid from top to bottom [fol. 142] of the trench, and that where any pick rock was shown the entire excavation had been calculated as pick rock.

It is difficult to imagine a condition where a contractor would make a competitive bid on rock excavation, or where a company would pay for rock quantities excavated, on any such basis, particularly when the unit price for shoot rock has been developed by Eastman at $7.38 per cubic yard, and pick rock at $4.01 per cubic yard. It is a matter of common knowledge that rock, both solid and loose, may be found from top to bottom in trenches, or it may carry an overburden of earth and only a few inches of rock show in the lower part of the pipe-line ditch. The matter of calculation of such excavation, where paid for by unit prices for earth and for rock, may readily become a matter of argument between the contractor and the company. In the case of Line "G" between Wichita and Ottawa, the company contracted with Mr. Jones, a pipe-line contractor of fourteen years' experience who has in that period constructed pipe lines involving the expenditure of about $20,000,000 for labor, to unload, haul, string and lay the pipe, excavate the ditches, including shoot rock and pick rock, backfill and test the line, for $0.59 per running foot. It is presumed that before making any such bid the contractor

informed himself concerning the kind of excavation he would likely encounter in the 130 miles of line; he testified that he received a total of $895,985.67 for this contract and that he lost $128,000 on it, but he did not allocate any part of this loss to pipe unloading, hauling, stringing, ditching, backfilling, or to the other operations for which he received unit payments in addition to the $0.59 per foot, and which amounted to $516,287 in addition to the $379,699 paid for the operations included in the $0.59 per foot bid. Mr. Jones testified that the reasonable cost per lineal foot for excavating solid rock would be "a little over 75 cents" in a ditch 28 inches by 40 inches. Such a ditch contains 7.8 cubic feet of excavation per lineal foot of ditch, and the cost of solid-rock excavation per cubic foot may then be taken as 9.62 cents. Mr. Jones' reasonable cost for excavation of solid rock in a ditch of this kind then becomes 27 times 9.62 cents or $2.60 per cubic yard. This price compares with Mr. Eastman's price of $7.38 per cubic yard for shoot-rock excavation, and his price of $4.01 per cubic yard for pick-rock excavation. Mr. Jones' testimony concerning reasonable costs for solid-rock excavation was made after the completion of this contract.

Mr. Black's testimony with respect to classified excavation was that he determined the percentage of such excava- [fol. 143] tion by observation of the territory through which the major part of these lines passed, and from his knowledge of the territory gained through more than twenty years' experience; he testified that he made a personal inspection of Line "G" from Wichita to Ottawa, and that he had allowed $2.50 per cubic yard for all classified excavation, whether solid or loose rock, and had allowed this amount in addition to ordinary cost of trenching and backfilling of ditches of the same dimensions. This average allowance of Mr. Black's for solid and loose rock is ample when considered with Mr. Jones' testimony of $2.60 per cubic yard for solid-rock excavation only.

If we assume that Mr. Eastman's classification of shoot-rock and pick-rock excavation is correct, it appears that he has used 2.8 times as much as he would have used for shoot-rock excavation on the basis of Mr. Jones' cost, and 2.9 times Mr. Black's cost. His allowance for pick-rock excavation cannot be compared with Mr. Jones' development for cost of solid-rock excavation excepting in so far as it

is $1.41 per cubic yard in excess of the allowance Mr. Jones made for solid-rock excavation. It is also $1.51 per cubic yard in excess of Mr. Black's allowance for both shoot and pick rock. In view of this apparent discrepancy between the developed prices of Mr. Eastman for rock excavation, and the reasonable prices testified to by Mr. Jones, and the prices developed by Mr. Black out of experience and rock excavation costs on contracts supervised by him in Oklahoma, Kansas and Missouri, we think but one logical conclusion can be drawn and that is to adopt the prices developed by Mr. Black.

Mr. Eastman compared labor costs to the company with labor costs used by Mr. Hamilton in exhibit 17, and by Mr. Black in exhibit 41, on eleven major pipe lines, as shown by the following tabulation:

| Line | Company Labor | Hamilton | | Black |
|---|---|---|---|---|
| | | Labor | Labor and Couplings | Labor and Couplings |
| Hutchinson-Superior | $355,893 | $382,744 | $429,343 | $348,436 |
| Fort Scott 8" | 202,184 | 180,961 | 194,736 | 139,639 |
| Springfield 10" | 380,394 | 442,570 | 489,809 | 343,085 |
| St. Joseph 12" | 144,683 | 164,621 | 190,224 | 157,268 |
| Quapaw 16" (new) | 52,809 | 43,147 | 51,841 | 53,842 |
| St. Joseph 16" (new) | 62,244 | 48,746 | 53,582 | 43,803 |
| Southern Trunk 16" (new) | 95,548 | 95,622 | 111,172 | 86,459 |
| Topeka 16" | 180,345 | 166,415 | 192,177 | 144,869 |
| Dilworth-Wellington | 174,894 | 162,915 | 176,595 | 163,799 |
| Ottawa-Law. Jct. 20" | 175,005 | 151,602 | 177,072 | 142,050 |
| Pampa-Wichita 20" | 1,547,013 | 1,832,822 | 2,210,633 | 2,052,519 |
| Total | $3,371,012 | $3,672,165 | $4,277,184 | $3,675,769 |

To make the company's total for the eleven lines comparable with Mr. Black's total, we have arrived at the cost of couplings and welds in these lines by deducting Mr. Ham- [fol. 144] ilton's allowance for labor of $3,672,165 from his allowance for labor, couplings and welds of $4,277,184, giving $605,019 for couplings and welds; adding this to the company total labor of $3,371,012, we have $3,976,031 as the company labor total, including couplings and welds, and the comparable totals become:

| | |
|---|---|
| Company labor costs plus— | |
| Hamilton's couplings and welds | $3,976,031 |
| Hamilton—labor cost, including couplings and welds | 4,277,184 |
| Black, labor cost, including couplings and welds | 3,675,769 |

Mr. Hamilton's valuation was therefore $301,153 more than the cost to the company when including $605,019 al-

lowed by Mr. Hamilton for couplings and welds, or 7.57 per cent above the company cost. Mr. Black's total allowance for the same items was $300,265 less than the cost to the company when including in the company total the $605,019 allowed by Mr. Hamilton for couplings and welds, or 7.55 per cent less than the company cost.

These comparisons would have been very materially changed had the tabulation included other major lines, or even one major line, such as line G, from Wichita to Ottawa, and which was constructed later than the Pampa-Wichita line included by Mr. Hamilton in the tabulation. The following tabulation shows this addition:

| | Company | Hamilton | Black |
|---|---|---|---|
| Total of eleven lines | $3,976,034 | $4,277,184 | $3,675,769 |
| Line G | 895,986 | * | 1,088,341 |
| | $4,872,020 | ..... | $4,684,110 |

* Totals not available.

On this basis Mr. Black's value is $187,910.00 or 3.86 per cent less than the company cost, instead of 7.55 per cent on the basis of the eleven lines tabulated by Mr. Hamilton. It is, therefore, apparent comparisons of parts of accounts do not truly reflect the differences in these valuations, for the result will vary in accordance with the lines selected. The only proper comparison is on the totals of these accounts, which are shown in the following tabulation:

| | | Hamilton | | Black |
|---|---|---|---|---|
| Total of account 1314 | ..... | $4,447,806 | ..... | $3,548,102 |
| Total of account 1333 | ..... | 46,893,014 | ..... | 43,099,711 |
| Total both accounts | ..... | $51,340,820 | ..... | $46,647,813 |
| Deduct pipe | $28,684,477 | ..... | $27,333,912 | ..... |
| Deduct classified excava. | 3,890,281 | ..... | 1,270,115 | ..... |
| | | 32,574,758 | | 28,604,027 |
| Totals remaining | ..... | $18,766,062 | ..... | $18,043,786 |

This tabulation shows that Mr. Hamilton's valuations for both of these accounts covering all labor and materials, exclusive of pipe and classified excavation, was $722,276 in excess of Mr. Black's valuation. Mr. Hamilton's labor [fol. 145] and coupling costs on the eleven major lines tabulated by him exceeded company labor and coupling costs 7.57 per cent, and on the totals of accounts 1314 and 1333, as shown by the above comparison, exceed Mr. Black's valuation 4 per cent; if Mr. Hamilton's excess of 7.57 per cent,

developed on the eleven major lines, is a fair measure of his excess over company cost on the labor in these two accounts, 1314 and 1333; it may also be argued that Mr. Black's valuation for these two accounts is 3.57 per cent higher than cost to the company, if such costs were comparable to the period in which these eleven major lines were constructed. However, we do not think these eleven lines were constructed in a period when material prices were comparable to 1931 prices, and for that reason we are of the opinion Mr. Hamilton's general labor and materials costs are excessive.

The major items of difference in the valuations of these two accounts, 1314 and 1333, are in classified excavation and in pipe. The testimony of the company's witness, Mr. Jones, taken in connection with that of Mr. Black, is conclusive with respect to the fair price of rock excavation. Mr. Black allowed a total of 508,046 cubic yards of rock excavation in these two accounts; Mr. Hamilton, estimated 514,468 cubic yards of pick rock and 247,596 cubic yards of shoot rock. Mr. Eastman's testimony that wherever encountered, pick rock and shoot rock were calculated from top to bottom of the ditch, as well as the effect of such computations when applied to line "G" (Black's exhibit 77), leads us to the conclusion that little if any weight should be given either his calculations of quantities of rock, or the price per cubic yard developed by him and applied to those quantities. We are of the opinion that Mr. Black has made an ample allowance for rock excavation in both Accounts 1314 and 1333.

As heretofore stated, one of the major differences in Accounts 1314 and 1333 is the allowance for pipe used in field and transmission lines. Considerable testimony was given concerning the base price of pipe, delivered prices of pipe, difference in prices of standard plain-end gas-line pipe, seamless pipe, screw pipe, electric-weld pipe, pipe of twenty-foot lengths, thirty-foot lengths and forty-foot lengths, and pipe with double bell ends. Testimony was offered also concerning the effect of freight rates to various points in the territory covered by the transmission system of the company, and also to show that the price of pipe at any given point was competitive; or, in other words, that whether shipped to Oklahoma City from Chicago or Lorain, it would have the same price per foot at Oklahoma City.

[fol. 146] This means the mill price of the pipe would vary, for, obviously, the freight from mill to point of delivery would remain constant for a given point.

Mr. Hamilton's pipe prices are all based on pipe from the Chicago district delivered f. o. b. Cambridge, Kan., on the assumption that freight from the Chicago district to Cambridge would be the average freight cost for all points on the system. Mr. Black's pipe prices are predicted on shipments from Lorain with freight added to point of delivery. Mr. Black's testimony is that the freight rate of 84 cents per 100 pounds from Lorain to Cambridge, Kan., is the same as it is to all points on company lines south of Cambridge in Oklahoma, and to points southwest in Texas on the lines of this company; that the Lorain rate is 61½ cents per hundred pounds in the Kansas City district; that it is somewhat higher at points along the lines of the company in northern Kansas and Nebraska. He, therefore, made a weighted average freight rate from Lorain for the entire state of Kansas, by applying the rates at various points to which pipe would be shipped to the weight of pipe which would be delivered at such points and arrived at a weighted rate for the state of 77 cents per 100 pounds. Nebraska was divided into two districts because of the variation of rates in the Superior district and Falls City district, and average rates were applied to pipe within those districts. Missouri was divided into two districts, one being the northern part of the state and the other the southwestern portion, and the average freight rate for each district was applied to pipe delivered therein. The difference between these weighted freight rates and the Lorain-Cambridge freight rate is $387,246. In other words, pipe in the system shipped from Lorain to Cambridge as a central point costs $387,246 more for freight than if shipped to the points at which used, at the freight rates applying to those points. Obviously the pipe was not shipped Cambridge but to the rail points nearest the point of use. If pipe prices are competitive at a given point, regardless of its point of origin, and the testimony is to that effect, it seems clear that by Mr. Hamilton's method of considering Cambridge the common point of delivery he has overpriced the pipe in his valuation by $367,246. The freight rates from the Chicago district to Cambridge were 58½ cents per 100 pounds, 69 cents to Amarillo and points

on the Tampa-Wichita line, 64½ cents to Oklahoma City, 35 to 43½ cents at Missouri points, 58½ to 77 cents at Kansas points and 35 to 61½ cents at Nebraska points.

In order to arrive at the true difference between pipe [fol. 147] prices in Mr. Hamilton's valuation and his own by calculating the pipe at a common delivery point, Mr. Black introduced exhibit 83, which is a summary of pipe in all gathered and transmission lines of the company, classified with respect to kind of pipe, total footage, total weight and total costs f. o. b. Cambridge, Kan., at Hamilton's prices and at Black's prices. This summary shows Mr. Hamilton's allowance for pipe f. o. b. Cambridge, Kan., totaled $27,318,551, while Mr. Black's allowance on the same quantity of pipe at Cambridge was $26,773,999, a difference of $544,552. This difference amounts to $1.51 per ton. The testimony developed the fact that this difference in price per ton appeared to be a reasonable difference in pipe prices, particularly when one considered the basis on which these prices were obtained by the company; that is, letters to the manufacturers of pipe asking them to quote on the delivery of approximately 359,700 tons of pipe of various kinds in the system.

There was some difference of opinion as between Mr. Hamilton and Mr. Black as to the cost of some pipe, especially screw pipe. The testimony was to the effect that plain end pipe cost less to buy and to lay and was less subject to leakage and depreciation than screw pipe. It appears that screw pipe costs more than plain end because the former has become obsolete, is not generally used and is not readily available. While screw pipe should be subject to depreciation to cover these factors we are not making any deduction therefor in the absence of any testimony as to the extent of such deductions. We find that the cost of pipe is $27,318,551 as included by Mr. Hamilton in his appraisal which is the price f. o. b. Cambridge, from which should be deducted $387,246 for excess freight included by Mr. Hamilton when he considered Cambridge, Kan., as a central shipping point instead of calculating freight to actual point of destination where pipe would be unloaded, which results in an allowance for this material of $26,931,305.

Exhibits 4, 5, 6, 7 and 20, all dealing with present conditions of pipe lines in Account 1333, were introduced by

the company. Exhibit 4 is a map showing the pipe-line system of the company, on which was indicated the location of various inspections. Mr. Hamilton referred to a total number of 17,700 inspections of the pipe lines of the company. Mr. Hancock testified 17,746 inspections had been made on the property and that this meant an average of one inspection for each 1,300 feet of pipe line. He also testified that 16,330 of these inspections had been made in the routine maintenance work of the company. On cross-[fol. 148] examination Mr. Harcock testified that 7,130 of these inspections had been made on the St. Joseph 16-inch line in a length of approximately 200 miles; that 6,667 of these inspections had been made in the approximately 50-mile length of line between Garnett and Ottawa, Kan., and furthermore, 6,667 of these inspections were made in 1927, and that the additional four years' life between 1927 and 1931 meant nothing when considering the present per cent condition of the line, because the added four years of depreciation would not be ascertainable by inspection. From this testimony it appears clearly that these 13,797 inspections made on approximately 250 miles of pipe line should not be seriously considered in a general average of inspections over the entire system, and should be given weight only on that section of the line on which they were made.

Mr. Hamilton testified that 506 inspections were made by engineers for the company accompanied by engineers for the Commission and that 822 additional openings were made by the engineers for the valuation department. Mr. Biddison testified that he made 142 inspections and that he thinks he reached a fair conclusion as to the system as a whole by these 142 inspections. In response to cross-examination he testified that the per cent condition applied to certain lines in the system did not reflect his judgment, inasmuch as the per cent condition applied by engineers for the company were different than those arrived at by him.

Mr. P. J. Richards testified to having analyzed 101 soil samples taken along the lines of the company, and having determined that 2 per cent of the line would last two to six years, 2 per cent six to twelve years, 12 per cent less than twenty years, and the remaining 84 per cent would last fifty years. He also testified that he could not determine the per cent condition of pipe by his method, but that he

could and did determine the life expectancy by a comparison of analyses of soils along the lines of the gas company's system, with the analysis of a soil in which the Bureau of Standards had buried pipe and which pipe was removed from time to time and the effect of the soil noted. He testified that his calculation was based on bare pipe. Most of the pipe in the system is either wrapped or painted and Richard's calculation on bare pipe would not be applicable. He had made no calculation on the per cent condition of the property.

Prof. A. M. Ockerblad testified with respect to laboratory tests he had made on coupons cut from pipe lines in the [fol. 149] transmission system of the company, in order to determine the tensile strength of the pipe. Inasmuch as there is no contention on the part of the state that inferior pipe has been used in the construction of this system, and no claim has been made that the system was overbuilt with respect to heavier pipe than was required, nothing will be gained by discussing Professor Ockerblad's tests.

Engineers from Mr. Black's office accompanied the engineers for the Cities Service Gas Company on an inspection of 506 inspection pits scattered over the entire pipe-line system. These inspections and Mr. Black's calculations were not weighted with the 16,330 inspections made by the company in the maintenance work on the system.

After considering the testimony of witnesses in respect to present conditions of the pipe lines, we are of the opinion that a condition of 90.1 per cent as testified to by Mr. Black apparently represents the average condition and have adopted that percentage.

It appears that Mr. Black had originally included in his valuation an item of $82,976 for paint on the Pama-Wichita line. This item was omitted by Mr. Hamilton, and Mr. Black's valuation corrected accordingly. However, it later appeared that Mr. Hamilton's omission was incorrect and that this item should be included and added to Mr. Black's value.

After giving consideration to all of the testimony and the exhibits relating to Transmission Line Equipment, Account No. 1333, we find that the reproduction cost new of this equipment was $43,746,298 and that the reproduction cost new less depreciation was $39,422,331.

Account No. 1334

Transmission—Other Equipment

This account is valued by Mr. Black at $6,938 new, and $5,633 depreciated. The account consists of water wells, tanks, and pumping equipment and station-lighting equipment at Cutton Valley, Drumright, Oklahoma City and the Seminole 16-inch junction in Seminole county.

This account is valued by Mr. Hamilton at $8,334 new, and $6,835 depreciated.

We find the present fair value of this account to be $5,633.

[fol. 150] Account No. 1379

General—Other Structures

In general, the account covers dwelling, garages, office building, warehouses and miscellaneous structures not classified under Accounts 1310, 1311, 1328 and 1330.

This account is valued at $117,396 new and $94,687 depreciated and we find the present fair value of this account to be $94,687.

Account No. 1384

General—Garage Equipment

This account covers all autos, trucks, trailers, garages, tools and equipment owned by the company. The account is valued by Mr. Black at $174,139 new and $74,481 depreciated.

The inventory of the company for this account was accepted by Black. Automobiles, trucks and similar equipment was priced by him but other equipment prices fixed by the company were accepted by Black.

This equipment is valued by Mr. Hamilton at $164,391 new, and $81,448 depreciated.

Mr. Black reaches a value new of $9,748 in excess of Mr. Hamilton's value. The difference is accounted for by the fact that Mr. Black priced the automobiles and trucks included in this account through dealers, without having knowledge of the special discount available to the Cities Service Gas Company in purchasing such equipment, while

Mr. Hamilton gave consideration to such discounts. We feel that it cannot be disputed, therefore, that the valuation found by Mr. Hamilton reflects more accurately what it would actually cost the company to reproduce these cars. Mr. Black found a depreciated value of $6,962 less than that of Mr. Hamilton. Without weighing the merits of the manner of arriving at the depreciated condition, but considering the fact that Mr. Hamilton used special discount figures in arriving at his cost new, we find that his depreciated cost of $81,448 should be used in the valuation as the present fair value of this account.

Account No. 1386

General—Telephone and Telegraph System

This account covers telephone and telegraph lines used by the gas transmission system of the Cities Service Company. The account is valued by Mr. Black at $480,641 new [fol. 151] and $410,999 depreciated. Mr. Hamilton's value is $535,493 new and $486,182 depreciated.

The inventory supplied by the company was accepted by Mr. Black as correct without check. The account was priced by quotations from manufacturers for materials, and installation costs were calculated by Mr. Black.

The company questioned the value priced on two towers at the crossing of the Arkansas river and introduced exhibits 55 and 56, showing that the actual cost of these towers and foundations in 1927 was $5,000. Because of lack of time Mr. Black did not make an inspection of these towers and the values were fixed on the description furnished by the company. Apparently, the value on this account should be increased by $4,285 to take care of the difference in the reproduction cost new of this item. Depreciating this added amount at the rate used by Mr. Hamilton gives $4,071 as the amount to be added to Mr. Black's present fair value of $410,999.

We find the present fair value of this account to be $415,070.

Engineering and Superintendence

Valuation witnesses for both the company and the Commission estimated engineering and superintendence during

construction at an amount equal to five per cent of physical property after excluding certain general accounts which would not require engineering.

Mr. Black testified that his allowance for engineering and superintendence was intended to cover all details of supervision and engineering in the location of pipe lines, preparation of plans and specifications, general engineering and supervision of construction, preparation of estimates, inspection and testing of materials and equipment, except some inspection and testing of pipe for which he had made allowances otherwise, and all other work usually carried on by an engineering organization on construction projects.

Mr. Hamilton stated that his estimate included engineering and superintendence of design, supervision of construction from an engineering standpoint, including superintendence as to the feasibility of the project, determination of quantities of gas to be delivered, size of pipe necessary, amount of production necessary to handle the load, determination of location, the compressor stations required and engineering in testing equipment after installed. He testified he arrived at his estimate of engineering and superintendence by applying 5 per cent to physical property values as he had estimated them.

[fol. 152] In view of the testimony of both witnesses that engineering and superintendence should be estimated at an amount equal to 5 per cent of physical property except certain items of general equipment, we find that allowance for engineering and superintendence during construction should be based on five per cent of physical property valuation excepting as to Accounts 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387 and 1388, which would require no engineering. We find the cost new to be $3,218,585, and the depreciated value to be $2,881,000.

## Taxes During Construction

Mr. Hamilton computed taxes during construction at $769,174, which he estimated based on 1 per cent of the physical property and on a construction period of two years, and did not depreciate such allowance.

Mr. Black estimated taxes during construction by finding the amount of taxes actually paid by the company for one year and converting the tax payment into percentage of

total depreciated cost of reproduction and used that percentage in estimating taxes during the construction period. This percentage was applied to a two-year construction period and we have adopted Mr. Black's estimate based on the actual experience of the company, which results in an allowance of $875,171, in the cost of reproduction new and $778,044 in reproduction cost new less depreciation.

## Interest During Construction

Mr. Hamilton allowed $6,337,386 for interest during construction, which he does not depreciate, and he testified that it was based upon an allowance of 8 per cent on a two-year construction period, "and put it in at 8 per cent for one year." That is, he used a two-year construction period and allowed 8 per cent return on the investment during half the time on all of the property. He assumed that for the first two years during which the property was being constructed there would be no income.

Mr. Black's estimate of interest during construction was based on a two-year construction period at the rate of 6 per cent. He assumed that land and right of way would be acquired early in the construction period and allowed two years' interest, or a total of 12 per cent on land and right of way. He allowed interest during construction on all property plus engineering and superintendence, administration and legal expense and taxes during construction. He assumed that part of the system would be placed in operation [fol. 153] before the entire project was completed. He did not make any allowance for interest on bank balances during construction.

The evidence shows that six per cent is the rate which the company has actually paid on borrowed money other than bonds. On page 43 of their reply brief, respondents contend that the investor is entitled to the same return on his money during the period the plant is being constructed as he is allowed to receive after the project is placed in operation. "You have the same investor and the same money going into the project. Whatever is fair in one case must be in the other." This theory is not sound.

There is little relation to be found between a rate of interest to be allowed for the use of money borrowed or ad-

vanced in construction, and a rate of return on the value of property when subsequently put into public service. The latter involves the continuance of operation, and many other considerations. An examination of the decisions will disclose that interest during construction is never measured by the rate of return allowed. We find that an allowance for interest during construction based upon an interest rate of 6 per cent is reasonable and that an allowance should be made of $4,351,934 in cost of reproduction new and $3,883,282 in the cost of reproduction new less depreciation.

## Cost of Financing

Mr. Hamilton included in his valuation an item for cost of financing of $3,422,512 undepreciated. Mr. Hamilton stated that this estimate was based on 4 per cent of the total value including interest during construction. He further testified that the company would be put to no expense in selling securities to the Cities Service Company, but that he based his estimate on the value attributable to its ability to so place its securities without expense.

Mr. Hamilton's theory is that this company would come here without any capital and without credit, and that it would have to go out into the markets and entail great expenses in convincing somebody that had money that this would be a profitable enterprise, and that the company should be entitled not only to a fair return on the actual investment necessary, but would also be entitled to a return on the expense to which it would be put because of its improvident and impoverished condition.

Mr. Black made no allowance for cost of financing in his valuation, and we think properly so. This company is en- [fol. 154] titled to a fair return on the capital which it prudently invests in the enterprise and no more.

We are attempting to find present value, and we must assume a construction by persons financially able to construct. Otherwise, the more impecunious the organizers, and the more subject to excessive cost of procuring money, the greater would be the present value of the property. This matter has been disposed of in recent decisions.

In Minneapolis v. Rand (285 Fed. 818, 829) the United States circuit court of appeals said:

"The cost of financing is assumed upon the theory that a company, desirous of establishing such a plant, should not be possessed of sufficient capital to pay for the plant and should be compelled to borrow money by floating securities through brokers and should be exposed to large discounts if compelled to obtain money in this way. The fair value of the plant should not be estimated upon such a basis of impecuniosity and exactions, but upon the theory if used, of reconstruction, by those financially able to build the plant, paying reasonable prices therefor."

In Colorado Power v. Halderman (295 Fed. 178, 191) United States District Judge Symes said:

"A valuation is also claimed for marketing of securities. This is not a proper item."

We disallow the claim in its entirety.

## Working Capital

Mr. Hamilton estimated working capital requirements at $772,126, which he testified was equal to two months' operating expenses and one month's gas purchases.

Mr. Black based his estimate of working capital on one and one-half months' expenses, including cost of gas based on an annual outlay of $6,200,000, arriving at the round sum of $775,000 which we find to be reasonable.

## Material and Supplies

Mr. Hamilton used $548,096 for materials and supplies requirements based on the materials and supplies on hand September 1, 1931, according to the books.

Mr. Black used the average cost of materials and supplies on hand according to the books at June and September 1, 1931, of $509,400.

Respondents contend that $119,275 should be added to Mr. Black's valuation because of alleged omissions by him [fol. 155] of compressor station spare parts. Mr. Hamilton's testimony throws some light on this subject:

"Q. Materials and supplies, that is $548,096. What is that?

A. Oh, it is the warehouse materials that are carried on hand. It is pipe and fittings and compressor station repair parts, and various items of that nature."

Mr. Black's testimony was that his allowance of $509,400 for materials and supplies, was the average of the June 1, and September 1, accounts furnished him by the Commission's accounting department, and that if these items were included in materials and supplies on hand on the books of the company they are included in his valuation. There is nothing in the record to show Mr. Hamilton's allowance of $548,096 did not include these spare parts, his testimony is that it did so include them; Black properly used an average of the account on hand at two different dates, and this accounts for the difference between the allowances by Hamilton and Black. We believe that an average cost is more representative of average conditions than the cost for one day and that if Mr. Hamilton's value was so averaged it would approximate the value reached by Mr. Black. We find that $509,400 is a reasonable allowance for materials and supplies.

## Intangible Values

Although, perhaps, not strictly intangible as that term is restricted in valuation proceedings, the following are items not associated in either valuation submitted with the acual physical materials and structures:

Organization.
Administration and legal expenses.
Miscellaneous construction expenses.
Going value.

These items are more or less elusive, and the witnesses based their estimates mainly on percentages of other values. The allowances undepreciated included in the respective valuations follow:

| | Black | Hamilton |
|---|---|---|
| Organization | $482,754 | $384,586 |
| Administration and legal | 1,287,348 | 384,586 |
| Miscellaneous construction expenditures | ..... | 769,174 |
| Going value | 3,820,000 | 8,898,532 |
| Total | $5,590,102 | $10,436,878 |

These items will be discussed in the above order.

[fol. 156] Organization Expenses.

Mr. Black included in his estimate of value an item of organization expense equal to three-fourths of one per

cent of physical property value to cover preliminary organization and legal expenses, preliminary engineering and geological expense, organization expenses up to time construction begins, preliminary survey and market survey.

Mr. Hamilton included organization expenses at one-half of one per cent of physical items, including preliminary work of getting the organization together, incorporation expenses other than legal expenses, "and items of that nature," and he could not itemize and assign costs to any of the items.

We find an allowance for organization should be based three-fourths of one per cent of the physical value giving a cost new of $480,008, and the value is not depreciated.

Legal and Administration Expense During Construction.

Mr. Hamilton, witness for the company, estimated law expense during construction at the rate of one-half of one per cent of physical property and included legal expenses for incorporation, drawing of contracts and the type of work that must be done prior to and during the construction of the property, charter fees, tax stamps, and expenses that had to do with the issuance of securities. He stated that he was unable to break down this estimate and, "I have never been able to, one of these legal fees."

Mr. Hamilton did not have the history of the actual legal expenses incurred during the construction of the plant, but testified that they would be incurred in drawing contracts, damage claims and items of that kind.

Mr. Black's estimate of legal expenses was combined with an estimate of administration expenses during construction, and he estimated the aggregate of both at two per cent of the physical property. He tesified that the organization and legal expense covered the cost during the construction period of administering the general business of the company, including mainly administration and legal expense and part of the organization that eventually becomes a part of the operating organization of the company.

Mr. Hamilton did not depreciate legal expenses; Mr. Black depreciated his estimates based on cost to reproduce new. We find an allowance for legal expense during construction should be based one-half of one per cent of the

[fol. 157] physical values, including engineering, giving a cost new of $340,094 and a depreciated value of $304,084.

Miscellaneous Construction Expenditures.

Mr. Hamilton included $769,174 for miscellaneous construction expenditures consisting of office rent, office employees and "various disappearing items of that nature during the construction period," arriving at the amount by applying one per cent to physical property.

Mr. Black included such items in other accounts.

In view of the fact that Mr. Black included such items in other accounts, a great number of which has been adopted in this valuation, it is doubtful whether or not an allowance should be here made. We are, however, for the purpose of taking care of any miscellaneous expenditures, allowing 1 per cent of the physical values including engineering and find that the reasonable value is $680,187 for the cost new, and $608,169, as the depreciated value.

Going Value.

Going value is that uncertain and elusive item of additional value which it is said inheres in an "assembled and established plant, doing business and earning money, over one not thus advanced." That is, the material and labor entering into the construction of a public utility property has so much value as so many units of material and so many hours of labor. When, however, the material and labor become part of a completed going property they take on a new value, which is not only the aggregate of the cost of the material and labor, but is the value of a property as it exists in use and with its business established, as distinguished from a bare aggregation of units of property. This additional value does not include "good will" as good will is generally defined, nor is it a value based upon capitalized earnings or a capitalization of pioneer losses or past operating deficits.

Going value may be defined, we think, as "that amount by which the value of a utility plant in operation, with customers attached and an established revenue, exceeds the value of an exactly similar plant all ready to go, or going, without any customers or revenue, but so situated that the

acquisition of customers and revenues is a mere matter of time and ordinary adjustments."

The best measure of the going value is to be found in the cost of creating such going value. The cost would include such intangible values as organization and legal expense, [fol. 158] administration costs during construction, cost of training employees, cost of records, cost of attaching business, and possibly some allowance for interest during construction and on idle plant. The items of interest and depreciation might properly be omitted from consideration because an allowance for interest and depreciation on idle plant is simply a device for capitalizing early losses, and any loss of use of money during development may be given consideration in arriving at the fair annual rate of return.

Mr. Hamilton estimated going value by "just taken ten per cent of the physical value for this particular case, for that item" and "I have not itemized it in any way." He included "the cost of carrying pipe capacity that is idle a portion of the time until you get up to the load for which it was ultimately or for which it was designed."

The testimony shows that about half of this property has been constructed since January 1, 1927, and that a high rate of return has been earned on all of it, both during construction and on any idle part of it, and the cost of maintaining the idle plant has been included in expenses. Further, idle plant is included in the valuations submitted and a current return and depreciation based on it. It would be a clear duplication to include idle plant in the rate base the same as used plant is included and to allow an additional value for interest and depreciation on idle plant.

Further, the testimony clearly shows that the actual experience of this company has been that the plant has been extended to meet demands and no idle lines have in fact been carried.

Mr. Hamilton's estimate is of value rather than cost. "What I have included is the value of the business attached and operating, and yielding a revenue." In estimating value he considered "partially the cost of attaching business." The customers of this pipe-line system are, with very few exceptions, affiliated companies and there would be no cost of convincing those companies that they should buy gas from this pipe line instead of from a competitor.

He included in his estimate of going value the "time of the engineers and others in negotiating the contracts, but that, for a wholesale situation is a small item." While it is a small item he not only allowed for it in going value, but he also allows for engineering, legal and other expenses separately and in addition to going value.

"The largest cost is the excess capacity that you will have to have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on." This assumption is based on the theory that [fol. 159] the plant is not to be reproduced under existing conditions, but under some other conditions. Mr. Hamilton's hypothesis contemplates the destruction and wiping out of all the distribution systems, the substitution of coal and wood stoves for gas heating and cooking appliances, and then a long campaign running over years of time to induce people to throw away their coal and wood stoves and heaters and reinstall gas appliances.

Mr. Hamilton's concept of going value, which consists largely of interest and depreciation which he referred to as "cost of carrying pipe capacity that is idle," is based on the assumption that the longer a pipe is idle the greater becomes its value. In this case $8,898,532 greater.

Mr. Black considered going value "as being the difference between a plant all ready to operate and not operating, and a plant all ready to operate with customers attached." He estimated going value to include the following items:

Books and records.

Organization of the operating company.

Interest and depreciation on idle plant.

Mr. Black adopted the same theory as Mr. Hamilton in relation to cost of carrying idle plant. The overlapping of estimates is apparent. The estimates both include interest and depreciation on idle plant.

In considering the allowance for going value, we must take into consideration the general nature of the pipe-line company's business as disclosed by the general testimony of the witnesses. For the purpose of arriving at the reasonableness of the rate charged by the pipe-line company we are considering the reproduction of the pipe line and not the distributing plants. The distributing plants were available in most instances before the pipe line was con-

structed, having been placed there for the distribution of local gas and gas from other sources. If the pipe line system were to go out of business and be reproduced, the distributing plants would still be available. The cost of attaching distributing companies to a pipe line does not compare with the cost of acquiring and attaching customers to a distributing system. To a great extent, the burden of acquiring and attaching new customers is placed upon the distributing plants and not upon the pipe line company. From a consideration of all the testimony and the evidence we cannot find any great value to be placed upon going value in a pipe line system situated as the one now under consideration. We find, therefore, that $2,000,000 is an ample allowance for going value based upon the general [fol. 160] testimony of the witnesses, giving consideration to the inclusion by the witnesses of interest and depreciation on idle plant and the very apparent fact that a large number of the elements of going value have been considered and included in other items of value.

The Fair Value of Gas Leases Used and Useful

The company owned as of September 1, 1931, gas leases covering 1,262,361 acres of land situated in Kansas, Oklahoma, Missouri and Texas. (Ex. 40.)

These leases grant to the lessee the right to drill for and take oil and gas, and generally (with some exceptions), run for a period of ten years from date, after which, if oil or gas is not then being produced they expire, otherwise they run so long as oil or gas is produced. The leases in general require the payment of rental until development and require the lessee, after development, to pay to lessors a royalty of one-eighth of the oil and gas. The company owns only the gas rights in these leases, the oil rights being held in most cases by affiliated companies.

These leases have been classified into developed, proven, probable and prospective.

"Developed" leases are those on which gas is actually being produced.

"Proven" are those adjacent to production, which will be drilled and on which it is considered gas will be found.

"Probable" consists of acreage adjacent to proven acreage having favorable geological structure, but which has not been completely tested.

"Prospective" consists of all other acreage. (Davis, Ex. 3, p. 7.)

The acreage owned by the company, and respondents classification of them is as follows (Ex. 40):

| | Developed | Proven | Probable | Prospective A | Total |
|---|---|---|---|---|---|
| Texas | 22,000 | 72,730 | 24,647 | | 119,307 |
| Hugoton (Kan. & Okla.) | | 123,440 | | | 123,440 |
| Okla., Kan. & Mo. | 20,207 | | 1,000 | | 21,207 |
| Okla., Kan. & Texas | | | | 908,287 | 908,287 |
| | 42,207 | 196,170 | 25,097 | 908,287 | 1,262,361 |

The same leases (excluding the Kansas, Oklahoma and Missouri, proven and probable) are classified by F. G. Holl, for the Commission, as follows:

## Amarillo Field

| | Acres | |
|---|---|---|
| Proved area: | | |
| Blocked | 60,940 | |
| Unblocked | 33,767 | |
| Total | | 94,707 |

[fol. 161]

## Hugoton Field

| | | |
|---|---|---|
| Proved area: | | |
| Blocked | 25,280 | |
| Unblocked | 59,087 | |
| Total | 85,367 | |
| Probable or semiproved areas | 32,008 | |
| Total | | 116,375 |

### Kansas, Oklahoma, Texas and Missouri

| | | |
|---|---|---|
| Favorable acreage: | | |
| Kansas | 132,202 | |
| Oklahoma | 91,317 | |
| Texas | 36,326 | |
| Missouri | 9,064 | |
| Total | | 268,909 |
| Prospective acreage: | | |
| Kansas | 364,659 | |
| Oklahoma | 248,208 | |
| Texas | 3,206 | |
| Total | | 616,073 |
| No value for gas: | | |
| Texas | 10,569 | |
| Oklahoma | 26,408 | |
| Kansas | 80,090 | |
| Total | | 117,094 |
| Grand Total | | 1,223,178 |

NOTE.—Proved and probable leases, Classes 1 and 2, in Kansas, Missouri and Oklahoma are not included in the above, excepting those in the Hugoton field of Kansas and Oklahoma. (Ex. 46.).

The company, ever since its organization, has produced less than half of the gas which it sells. In 1930 it purchased about 54 per cent and produced about 46 per cent.

It owns many gas purchase contracts which entitle it to the gas produced from certain leases in Kansas, Oklahoma, and Missouri, covering 782,421 acres of land and 1,502 wells.

The gas wells situated on the lands covered by these purchase contracts, the gas from which the company is entitled to take by paying the agreed price per M. c. f., have an open flow of gas of 2,138,170 M. c. f. per day (Ex. 3, Tables 16, 17).

The company claims that the fair market value of the gas rights in all of the leases owned by it is $12,914,189, exclusive of the value of the wells and equipment, while the evidence of F. G. Holl, for the Commission, places their fair market value at $4,473,659 (exclusive of the value of the proven and probable Kansas, Oklahoma, and Missouri lease, which the company places at $442,940), so that to obtain a comparable figure, there should be added to Holl's valuation $442,940, making his valuation $4,916,599.

The values of the leases given above do not include the [fol. 162] value of the wells and equipment of wells on developed leases, as claimed by the company at $1,953,149, and as here adopted at $1,811,596.

Of the 1,262,361 acres of leases owned by the company only 42,297 acres have been drilled or developed. The remaining 1,220,064 acres have not been drilled and are undeveloped.

## Amarillo Field

## (Texas)

The company owns gas leases covering 94,829 acres in what is known as proven sweet gas area in Texas, in the Amarillo field. This proven sweet gas area is a portion of a huge field in the Panhandle, and is approximately 130 miles long and from seven to forty miles wide. It contains approximately 1,001,785 acres.

Of the company's acreage in this field 22,090 acres are developed, having sixty gas wells thereon. The testimony of Ralph E. Davis, the company's witness, a gas engineer and geologist, who made a survey of the company's gas

holdings, is that the recoverable gas (gas reserves) from these leases situated in this proven area, and comprising 94,820 acres, is 15,000,000 cu. ft. per acre.

One of these Texas leases is the Burnett lease (Ex. 48). It covers 63,880 acres, and requires a minimum payment of $50,000 per year, in advance, for ten years whether or not gas is taken from the lease. For the first two years, the royalty is one-eighth of 3 cents per M for all gas taken; for the next three years, one-eighth of 3½ cents per M; for the next five years, one-eighth of 4 cents per M; thereafter one-eighth of 4 cents unless the price of gas at the well is increased, in which event the royalty is to be one-eighth of the weighted average price. The Burnett lease is not a solid block, there being within said lease other leases owned by others than the company, on which there are producing wells. Up to the present time the $50,000 annual payments required on this lease have exceeded the royalty earned on the gas taken.

The witnesses for the company placed the market value of these leases at from $45 to $125 per acre, the higher values being placed on the Burnett ranch and blocked acreage. Eight witnesses testified for the respondents, two of them were employees, and all of the remaining, save one, were connected with companies whose interest it is to place a high value on leases for rate-making purposes.

F. G. Holl, for the Commission, testified that the value of the blocked acreage, consisting of 60,940 acres, was $45 per acre, and that the value of the remainder of the proven [fol. 163] leases 33,767 acres, was $25 per acre. Holl testified that scattered leases in this field in Wheeler county in the vicinity where the largest wells in the entire field have been found could be purchased at $5 per acre, net to the purchaser, such leases covering both the oil and gas. That in Potter county, near where the largest wells have been found, on September 14, 1931, a lease which was about to expire was renewed at $8 per acre for 5,000 acres.

The evidence of respondents shows that in 1931 the company conveyed to the Texoma Natural Gas Company (an affiliated company) 59,788 acres of leases, including the Coon ranch of approximately 25,000 acres, which was blocked, at the price of $45 per acre. This acreage was all in the proven sweet gas area in the Amarillo field, and is comparable with the proven and developed leases retained

and now owned by the company. The evidence also shows that these leases so sold to the Texoma cost the company somewhat less than $15 per acre on the average. (Ex. 34, Tr. 454, 455.)

The books of the company also show that from January 1, 1930, to June 30, 1931, it purchased 21,158 acres of its leases in the Amarillo field in the sweet proven gas area, now valued by respondents at approximately $93 per acre, at an average cost of but $12.78 per acre. (Ex. 90.)

The evidence shows that there is a large oversupply of gas developed by gas companies and independent producers in the Amarillo field, which on account of the lack of market, cannot be sold, and that gas is being sold in this field at 2 cents per M. c. f. at the well. That in the Amarillo proven sweet gas area there are approximately 125 "shut-in" wells drilled and capable of producing gas which cannot be sold for want of a market, and that these "shut-in" wells have an open flow of 2,260,000,000 cu. ft. per day.

That the owners of wells are able to sell only a small per cent of their gas; that the Lone Star Gas Company has a pipe line into this field connected to 65 wells, from which the runs averaged during the first six months of 1931, a little over 100 M per day, for which the company paid 2 cents per M, or a royalty of $2 per day (less than interest on the cost of completing a well), and for that reason operators are not drilling any more wells or acquiring any more acreage. (Tr. 1920, 1921.)

From all of which we conclude and find that the fair market value of the developed and proven gas leases in the Amarillo field, owned by the company, as of September 1, 1931, does not exceed the following:

[fol. 164] Fair Market Value Leases—Amarillo Field

| [fol. 164] Developed and proven: | Acreage | Value per acre | Fair market value |
|---|---|---|---|
| Blocked acreage | 60,940 | @$50 | $3,047,000 |
| Not blocked | 33,880 | @ 35 | 1,185,800 |
| Totals | 94,820 | | $4,232,800 |

## Probable Acreage

The company owns 24,547 acres of gas leases in Texas situated outside of the proven sweet gas area, some of which are in the sour gas area.

The testimony of the witnesses for respondents as to the value of this acreage varied. Some stated that part of these are worthless (Freeman p. 593); others at from $5 to $25 per acre.

F. G. Holl, for the Commission, placed the fair market value of the gas rights in that part of this acreage which he classed as "favorable" at $1 per acre and 50 cents per acre for that part which he classes as "prospective," and nothing for the remainder of the Texas acreage. (Ex. 46.).

We find from the evidence that the average fair market value of the gas rights for this 24,547 acres classed by respondents as "probable" does not exceed $2 per acre, and that the fair market value of such acreage does not exceed $49,094.

## Hugoton Field

### (Kansas and Oklahoma)

The company owns 123,440 acres of gas leases in the Hugoton field situated in northwestern Oklahoma and southwestern Kansas, all of which it contends are "proven." (Ex. 40.)

This is another enormous gas field estimated to comprise 4,000,000 acres of gas-productive lands. Its limits are not yet defined. They can be determined only by additional drilling. Dr. Raymond C. Moore, state geologist, estimates the gas reserves in this field as sufficient to supply all of the state of Kansas, on the basis of that now used in Kansas, for a period of over 100 years. (Tr. 1964, Ex. 47.) There is a market for but a small portion of the developed gas in this field. Little drilling has been done, but there is sufficient drilling to demonstrate that this is a rich field of gigantic proportions.

Of the company's acreage, F. G. Holl, for the Commission, classified 84,367 acres as "proven," 32,008 acres as "probable" and the remainder as "prospective."

[fol. 165] Ralph E. Davis, for respondents, gave it as his opinion, as a result of his geological survey made for respondents, that the recoverable gas from the "proven" area of this field is 10,000,000 cu. ft. per acre, and from the "probable" at 7,000,000 cu. ft. per acre. (Table 1, Ex. 3.)

There is no development and no wells on any of the company's acreage in the Hugoton field. The company's leases

consist of one large lease, the Stonebreaker lease, covering 25,280 acres, and over 500 smaller leases. The terms of each of these 500 leases require the drilling of a well within ten years from its date; otherwise, the lease expires at the end of ten years. The cost of a well in this field is over $25,000, and if the company is to hold these leases it will have to drill at least 500 wells within eight years from this date, that is, before 1940, at a cost of $12,500,000, or said leases undrilled will expire. The company has no pipe line within ninety miles of these leases. (Tr. 1019.)

Witnesses for respondents, four in number, testified that the fair market value of the gas rights in these leases, which are in the proven area, is from $3 to $10 per acre, and the respondents claim that the fair market value of their 123,440 acres of leases is $1,172,680.

Against this is the testimony of F. G. Holl that leases for oil and gas could be purchased in the proven area of this field at the time of the hearing at $1 to $2 per acre; that the Derby Oil Company had within sixty to seventy days prior to his testimony, purchased 5,947 acres of leases in this proven area at $1 per acre (Tr. 1958) and that the fair market value of these leases is:

Hugoton Field

| Proved area: | Acres | Per acre | Fair market value |
|---|---|---|---|
| Blocked | 25,280 | @$7 50 | $189,600 00 |
| Unblocked | 59,087 | @ 1 50 | 88,630 50 |
| Probable area | 32,008 | @ 1 00 | 32,008 00 |
| Prospective area | 7,065 | @ 50 | 3,532 50 |
| Totals | 123,440 | | $313,771 00 |

We find that the fair and reasonable value of this 123,440 acres is not in excess of the following:

Fair Market Value Leases—Hugoton

| | Acres | Per acre | Fair market value |
|---|---|---|---|
| Proven (blocked) | 25,280 | @$7 50 | $189,600 00 |
| Proven (not blocked) | 59,087 | @ 5 00 | 295,435 00 |
| Probable | 32,008 | @ 2 00 | 64,061 00 |
| Prospective | 7,065 | @ 1 00 | 7,065 00 |
| Totals | 123,440 | | $556,116 00 |

[fol. 166] Kansas, Oklahoma and Missouri

(Exclusive of Hugoton Field)

Proven and Probable

Ross Stuntz, superintendent for the company, testified that the company owned, in Kansas and Oklahoma, proven and developed and probable acreage, of the fair market value as follows (Tr. 717-719):

| Proven and developed: | Acres | | Fair market value | |
|---|---|---|---|---|
| Kansas | 16,125 | | $138,240 | |
| Oklahoma | 4,082 | | 239,700 | |
| Totals | | 20,207 | | $377,940 |
| Probable acreage: | | | | |
| Kansas | 80 | | $8,000 | |
| Oklahoma | 980 | | 57,000 | |
| | | 1,000 | | 65,000 |
| Totals | | 21,207 | | $442,940 |

(Tr. 935)

There was no other evidence as to the value of this acreage, and it is accepted as correct.

Prospective Acreage

This acreage is scattered throughout Texas, Oklahoma, Kansas and Missouri. Very little of it is within the reach of the company's pipe lines. From its location it is probable that its value, if any, is for oil and not gas.

From July 1, 1931, to October 1, 1931, the company surrendered 61,471 acres of prospective acreage, as not of sufficient value to warrant payment of rentals. (Ex. 43.)

The acreage of the company's prospective leases, as classified by Mr. Nesbit, chief geologist for respondents, is 998,287 acres, which he values at $2 per acre. (Ex. 30.)

Ralph E. Davis, for respondents, classifies 1,031,127 acres of the company's leases as "prospective" and values them at $1 per acre.

F. G. Holl, for the Commission, classifies 268,909 acres as "favorable" and values them at $1 per acre, 616,073 acres as "prospective" at 50 cents per acre, and the remainder at no value.

The foregoing being for the gas rights only.

It is our conclusion that the value of the gas rights in these prospective leases is not in excess of $998,287.

The following is a summary of what we believe the fair weight the evidence shows is the classification of all of the gas acreage of the company. We also find that the fair [fol. 167] value of all the acreage of the company, exclusive of the value of the wells and well equipment, is not in excess of the amounts set forth below.

## Summary

### Fair Market Value of Gas Leases

| | Acres | Value per acre | Fair market value |
|---|---|---|---|
| **Amarillo Field (Texas):** | | | |
| Developed and proven: | | | |
| Blocked | 60,940 | @$50.00 | $3,047,000 |
| Not blocked | 33,880 | @ 35.00 | 1,185,800 |
| Total | 94,820* | ..... | $4,232,800 |
| Probable acreage | 24,547 | @ 2.00 | 49,094 |
| Total | 119,367 | ..... | $4,281,894 |
| **Hugoton Field (Kansas and Oklahoma):** | | | |
| Proven blocked | 25,280 | @ $7.50 | $189,600 |
| Not blocked | 59,087 | @ 5.00 | 295,435 |
| Probable | 32,008 | @ 2.00 | 64,016 |
| Total | 116,375 | | |
| Prospective | 7,065 | @ 1.00 | 7,065 |
| Total | 123,440 | ..... | $556,116 |

* Of the above, 22,090 acres are developed with sixty producing wells.

| | Acres | |
|---|---|---|
| **Kansas, Oklahoma and Missouri (exclusive of Hugoton):** | | |
| Proven: | | |
| Kansas, Oklahoma and Missouri | 20,207 | $377,940 |
| Probable: | | |
| Kansas, Oklahoma and Missouri | 1,060 | 65,000 |
| Total | 21,267 | $442,940 |
| Prospective: | | |
| All other except Hugoton | 998,287 | 998,287 |
| Total | 1,262,361 | $6,279,237 |

The value of all leases of the company, after deducting the value of leases canceled and surrendered, as shown by the books of the company, is (book value) $6,573,489.70. (Tr. C. H. Montgomery, Ex. 49.) Add value of wells and

well equipment, $1,811,596; total value of all leases and wells, $8,090,833.

## Gas Leases—Used and Useful

The amount of gas produced and purchased by the company for the year ending December 31, 1930, is as follows (Ex. 3, Table 10, p. 65):

| Gas purchased and produced: | M. c. f. |
|---|---|
| Gas produced | 34,401,978 |
| Gas purchased | 31,123,002 |
| Residue gas purchased | 8,638,965 |
| Total | 74,163,945 |
| Or on an average per day of (74,163,945 ÷ 365) | 203,189 |

[fol. 168] This is on an 8-oz. base, to reduce to a 2-lb. base, on which the measurement of the gas produced is based, this amount should be reduced by 9.2 per cent.

The peak load of the company's gas system was on January 16, 1930. On that day the companies used 330,000 M. c. f. of gas. (Tr. 905.)

The pipe lines of the company have no greater capacity than for this peak load (Tr. 244, 252) and there is little probability of any greater demand for gas than that produced and purchased by the company in 1930, for the reason that because of local gas, and the proximity of other pipe-line companies, the company's opportunity to extend its territory is limited.

The evidence shows that the company in the past and at the present time buys more gas than it takes from its own leases. In 1930 the company purchased about 54 per cent and produced about 46 per cent of the gas sold.

## Gas Reserves

The company owns purchase contracts for gas on leases in the Kansas and Oklahoma fields adjacent to its pipe lines which have wells, the open flow production of which is 2,138,170 M. c. f. per day. (Ex. 3, Tables 16 and 17.)

These purchase contracts cover 782,421 acres of leases and 1,502 gas wells. The total open-flow capacity per day

of the gas wells owned by the company, plus the gas to which it is entitled under its purchase contracts, is:

| Open flow per day: | M. c. f. |
|---|---|
| Amarillo, 60 wells, 22,090 acres (Tr. 449) | 1,532,625 |
| Kansas, Oklahoma and Missouri, 20,207 acres (Ex. 3, Table 3) | 258,837 |
| Add purchase contracts (Ex. 3, 82-96, Tables 16, 17) | 2,138,170 |
| Total open flow (available to company) | 3,929,632 |

The foregoing, 3,929,632 M. c. f., is the open-flow capacity per day of the wells owned by the company from 42,297 acres, all of its developed leases, plus the daily open-flow capacity of the wells situated on the leases covered by its purchase contracts.

The amount of gas which it is customary to take and which can be safely taken from a well is 20 per cent of its open-flow capacity, so that the amount of gas which is daily available from the company's purchase contracts and producing wells is 20 per cent of the daily open-flow capacity, or 785,926 M. c. f., which is more than 3½ times the average daily consumption of gas produced and pur- [fol. 169] chased and more than 2½ times the highest peak load and capacity of the company's pipe-line system.

From the foregoing it will be seen that the company now has available from its purchase contracts and from its developed leases in Kansas, Oklahoma, Missouri and Texas (42,297 acres of leases) 786,309 M. c. f. of gas per day, over 3½ times its average daily requirements, and 2¼ times its maximum requirements on the day of its peak load.

This leaves the company a reserve of 1,220,064 acres of leases which are undrilled, unused, and are not called upon to meet the company's requirements, as follows:

| Undeveloped leases: | Proven | Probable | Prospective | Total |
|---|---|---|---|---|
| Texas | 72,730 | 24,547 | ..... | 97,277 |
| Hugoton | 123,440 | ..... | ..... | 123,440 |
| Oklahoma | ..... | 980 | ..... | 980 |
| Kansas | ..... | 80 | ..... | 80 |
| All other | ..... | ..... | 998,287 | 998,287 |
| Total reserve acreage not developed or used | | | | 1,220,064 |

None of these 1,220,064 acres is drilled or producing. The Hugoton field, where the company owns 123,440 acres of undrilled proven leases (its classification) is approximately ninety miles from the company's pipe line. The number of separate leases in this field is over 500, all of which will expire in eight years unless drilled. This means that to hold these leases the company will have to drill over 500 wells at an expense of over $25,000 per well, or over $12,500,000, within the next eight years, and in addition pay a yearly rental in a substantial amount.

### Prospective Leases

The leases of the company classified by it as "prospective," consisting of 998,287 acres, are scattered. Very few are available to the company's pipe line.

Ralph E. Davis, geologist and gas engineer, witness for the company, who made an exhaustive study of the company's holdings, testified that the recoverable gas reserves in the company's leases in the Amarillo field is 15,000,000 cu. ft. per acre for the probable. In the Hugoton field, 10,000,000 cu. ft. per acre for the proven and 7,000,000 cu. ft. per acre for the probable, and stated that these figures are conservative. (Ex. 3, pp. 25, 27.)

On this basis, if the classification of Mr. Davis of the acreage is accepted, the gas reserves of the company in the acreage covered by the company's gas leases classified by [fol. 170] Mr. Davis as proven and probable, amounts to 2,448,664,000 M. c. f. (Ex. P. 34, Table 1, p. 36), exclusive of the 998,287 acres of leases classified by the company as "prospective."

If it be assumed that the company will annually require in the future as much gas in addition to that purchased as it required in the year 1930, its annual requirements from its gas leases would be 34,401,978 M. c. f. (Ex. 3, p. 65, Table 10), and its recoverable gas reserve represented by its leases, proved and probable, excluding all the prospective, would last for seventy-one years, plus.

On the same basis, the company's holdings in the Amarillo field alone would supply all of its requirements for fifty years, plus.

Or, if the company should disregard its purchase contracts and purchase no gas and take all of its requirements,

which for 1930 amounted to 74,000,000 M. c. f. (Ex. 3, p. 65, Table 10), from its proven and probable leases, its recoverable gas reserve, excluding its prospective leases, would last for thirty-three years, plus.

Or, if the company would surrender all of its leases except only the proven and probable, in the Amarillo field, and would cancel all of its purchase contracts, its Amarillo leases alone would supply all its requirements, 74,000,000 M. c. f. per year for twenty-three years, plus.

$$\frac{\text{Total gas reserve (excluding gas purchased)} \quad 2{,}448{,}664{,}000 \text{ M. c. f.}}{\text{Total gas produced, 1930} \quad 34{,}401{,}978 \text{ M. c. f.}} = 71 + \text{years}$$

$$\frac{\text{Total Amarillo reserve (excluding gas purchased)} \quad 1{,}726{,}650{,}000 \text{ M. c. f.}}{\text{Total gas produced, 1930} \quad 34{,}401{,}978 \text{ M. c. f.}} = 50 + \text{years}$$

$$\frac{\text{Total gas reserve (excluding gas purchased)} \quad 2{,}448{,}664{,}000 \text{ M. c. f.}}{\text{Total gas sold 1930 (Including gas purchased.)} \quad 74{,}000{,}000 \text{ M. c. f.}} = 33 + \text{years}$$

$$\frac{\text{Total Amarillo reserve (excluding gas purchased)} \quad 1{,}726{,}650{,}000 \text{ M. c. f.}}{\text{Total gas sold 1930 (Including gas purchased.)} \quad 74{,}000{,}000 \text{ M. c. f.}} = 23 + \text{years}$$

If the opinion of Mr. Nisbit, respondents' geologist, as to the classification of the acreage of the Hugoton field as to proven and probable, is accepted the amount of the company's gas reserve will be greatly increased as he classifies 123,440 acres in the Hugoton field as "proven," while Mr. Davis classified the company's holdings in the Hugoton field as 49,210 proven, and 28,070 as probable.

From the foregoing it will be seen that the company owns many more gas leases than are "used and useful" in the business of supplying gas to its consumers. It is a fair inference from the facts in evidence that the company acquired these excess leases expecting to sell them at an enhanced price. The evidence shows it did this in the sale [fol. 171] of 59,788 acres of leases to the Texoma in 1931, at a profit of over $1,000,000.

Of the leases owned by the company, 123,440 acres valued by respondents at $1,172,680 are in the Hugoton field. None of them is producing, none have been drilled. They are all approximately ninety miles from any pipe line owned by the company. The terms of the leases require the expenditure of over $12,500,000 within eight years for drilling to prevent their expiration, and also require the pay-

ment of a substantial amount yearly in rentals. The acquisition of these leases at the price the company paid for them was no doubt a wise business venture on which, when these leases are sold, a substantial profit should be realized, but they are not used or useful to the company in supplying the needs of its customers, nor can it be seen that they will be in the near future.

The same can be said of the 998,287 acres of nonproducing leases designated as "prospective." They are scattered, their value is speculative, very few are available to any pipe line owned by the company, and they are a source of expense in annual rentals.

In fact the company recognizes this fact as the evidence shows that it released and surrendered 61,471 acres of these leases between July 1, and October 1, 1931, as not worth the stipulated rentals.

The following gas acreage, consisting of 50,000 acres in the proven sweet gas area in the Amarillo field, 22,090 acres of which are developed, and all of the proven, developed and probable acreage situated in Kansas, Oklahoma and Missouri, 21,267 acres are, in our opinion, the only leases of the company which are used and useful and are sufficient for all the company's present requirements and for a sufficient reserve.

Used and Useful Leases

| | Acres | | Fair market value | Gas reserve M. c. f. |
|---|---|---|---|---|
| Kansas, Oklahoma and Missouri: | | | | |
| All developed, proven and probable leases in Kansas, Oklahoma and Missouri | 21,267 | | $442,940 | 35,424,000 |
| Texas-Amarillo Field: | | | | |
| Blocked | 45,830 | @$50 | 2,291,500 | ..... |
| Not blocked | 4,170 | @ 35 | 145,950 | 750,000,000 |
| Total | 71,267 | | $2,889,390 | 783,424,000 |

Of these 71,267 acres, 42,297 are producing and 28,970 acres are not developed, as follows:

| Proven Leases: | Acres | |
|---|---|---|
| Developed: | | |
| Texas | 22,090 | |
| Kansas, Oklahoma and Missouri | 20,207 | |
| Total | | 42,297 |

[fol. 172]

| | | |
|---|---|---|
| Undeveloped: | | |
| Texas—proven | 27,910 | |
| Oklahoma—probable | 980 | |
| Kansas—probable | 80 | |
| Total | | 28,970 |
| Total | | 71,267 |
| Total fair value of all leases (71,267 acres used and useful) | | $2,880,390 |
| Add value of all wells and well equipment | | 1,451,626 |
| Total value of leases, used and useful, including wells and well equipment | | $4,332,016 |

The gas reserve in these 71,267 acres according to respondents' testimony is 783,424,000 M. c. f. This is sufficient to furnish all of the company's requirements in addition to the gas purchased under its purchase contracts, on the basis of its requirements for the year 1930, for a period of 22 years, plus, as follows:

Gas Reserves in 71,267 Acres Allotted to the Company as Used and Useful

| | Acres | Gas reserve per acre | Amount of gas reserve M. c. f. |
|---|---|---|---|
| Amarillo proven | 50,000 | 15,000 M | 750,000,000 |
| Kansas, Missouri and Oklahoma, proven and probable | 21,267 | ..... | 33,424,000 |
| Total gas reserve | 71,267 | ..... | 783,424,000 |

(Ex. 3, pp. 25, 26, 27, 35.)

$$\text{Gas reserve 71,267 acres: } 783{,}424{,}000 \text{ M. c. f.} \div \text{Yearly requirement: } 34{,}401{,}978 \text{ M. c. f.} = 22 \text{ years, plus}$$

The sixty wells on the 22,090 acres in the proven sweet gas area in the Amarillo field included in the acreage allotted to the company as above, are capable of supplying 306,525 M. c. f. per day (20 per cent of open flow—1,532,625 M. c. f. ÷ 5 = 306,525 M. c. f.)

The maximum capacity of the company's pipe line from the Amarillo field, a 20-inch line, is but 125,000 M. c. f. per day. In other words, the sixty wells on the 22,090 de-

veloped acres in Amarillo field are capable of supplying over twice as much gas as the company has pipe-line capacity to take from the Amarillo field.

In arriving at the value of these 71,267 acres of leases allotted to the company as "used and useful" the fair market value of the Kansas, Oklahoma and Missouri acreage, as claimed by respondents in exhibit 40, is adopted.

These 71,267 acres here allotted to the company as used and useful include all of the company's developed leases, [fol. 173] wherever situated; also all of its proved and probable leases in Kansas, Oklahoma and Missouri (except the Hugoton field).

We find that all other leases owned by the company (1,220,064 acres) are not used and useful to the company in supplying gas to its customers. It would be inequitable to include the value of leases other than the 71,267 acres specified above, owned by the company in the rate base, or to charge, as costs of operation, the expense of carrying such excess leases.

The amount of gas reserve which a company should be allowed to carry for valuation purposes is best determined by its requirements. The records in this case are quite complete as to the requirements of the company. A gas company should not be allowed to speculate in gas leases and have its speculation financed by charges to its consumers. Neither should it be allowed to place in its valuation for the purpose of increasing its return, gas reserves over and above those necessary to serve properly its consumers. The gas company at a small cost has acquired gas rights which it now claims have a value of millions of dollars. We are interested only in those which are used and useful in the public service. We cannot see how any leases other than the 71,267 acres of leases designated above can be held to be used or devoted to the public service.

In the United Fuel Gas Company case the company asked that the value of its gas rights and leaseholds be fixed at $30,000,000. It was given a value of approximately one-fifth of that amount, based on the book value in the absence of any better evidence in the record.

In speaking of the value of the gas leases the court in the United Fuel Gas Co. v. Public Serv. Com., 14 F. 2d 209, said:

"The plaintiff, at a net cost of a few millions acquired rights which it claims have now a value of upwards of thirty, and which it might be difficult to deny were worth two-thirds of that sum. What proportion of this is presently used and useful in the public service? Roughly, four-fifths of the valuation it puts upon them is represented by gas which upon reasonable grounds it believes to be under land in which it has not yet operated and nearly two-thirds under acreage underneath which it has not yet been demonstrated that there is any gas, although its presence there is probable. Plaintiff is not to be criticized for acquiring these rights widely extended and largely untested as they are. In securing them it doubtless acted wisely, both from its own standpoint and from that of those who depend upon it for their supplies of gas. But is that of any present importance?

"It will be noted that the total of the gas underlying the proven acreage was 249,100,000 M. c. f. As the plaintiff [fol. 174] sells annually about 47,000,000 M. c. f., of which 10,500,000 goes to the West Virginia retail purchasers, it has under its proven territory gas enough for everybody for more than *five years*, and an amount sufficient to meet the needs of its public-service patrons alone for almost a quarter of a century.

"For the reason already stated, we cannot see how any other portion of its gas can be held to be used in the public service, no matter how elastic a definition be given to the word 'used.' At the risk of tiresome repetition, we can say that we do not criticize plaintiff for acquiring any or all of its gas rights. It was doubtless wise to get them. All that we decide is that, in arriving at the rate base upon which plaintiff is entitled to a fair return, we may not combine two opposing theories." (Italics ours.)

Neither do we criticize the pipe-line company for acquiring these gas leases. Their purchase was no doubt a wise speculation and the sales to the Texoma Natural Gas Company prove them to have been profitable, but property acquired for speculative purpose should not enter into the rate base. We find the fair market value of the gas leases (exclusive of wells and well equipment) used and useful in the system to be $2,880,390.

## Valuation Summary

The following is a summary of all the accounts entering the rate base:

| Acct. No. | Title | Cost of reproduction | Reproduction cost less depreciation |
|---|---|---|---|
| 1307 | Production rights of way | $55,982 | $55,982 |
| 1310 | Production field measuring station structures | 40,517 | 35,909 |
| 1311 | Production other structures | 59,087 | 47,876 |
| 1312 | Production gas well construction | 1,588,450 | 1,153,157 |
| 1313 | Production gas well equipment | 894,618 | 658,439 |
| 1314 | Production field line equipment | 3,548,102 | 3,126,159 |
| 1315 | Production field measuring station equipment | 302,611 | 205,746 |
| 1316 | Production drilling and cleaning equipment | 32,833 | 27,908 |
| 1317 | Production other equipment | 1,637 | 1,333 |
| 1325 | Transmission land | 145,202 | 145,202 |
| 1327 | Transmission rights of way | 1,057,530 | 1,057,530 |
| 1328 | Transmission compressing station structures | 1,608,151 | 1,406,102 |
| 1329 | Transmission measuring station structures | 147,337 | 133,310 |
| 1330 | Transmission other structures | 128,704 | 113,341 |
| 1331 | Transmission compressing station equipment | 8,954,220 | 8,048,910 |
| 1332 | Transmission measuring station equipment | 820,281 | 759,025 |
| 1333 | Transmission line equipment | 43,740,208 | 39,432,331 |
| 1334 | Transmission other equipment | 6,938 | 5,633 |
| 1376 | General other land | 3,055 | 3,055 |
| 1379 | General other structures | 117,306 | 94,687 |
| 1380 | General office equipment | 117,817 | 106,035 |
| 1381 | General store equipment | 2,123 | 1,805 |
| 1382 | General shop equipment | 26,991 | 23,084 |
| 1383 | General stable equipment | 640 | 568 |
| 1384 | General garage equipment | 104,391 | 81,448 |
| 1385 | General laboratory equipment | 8,369 | 8,202 |
| 1386 | General telephone and telegraph system | 484,926 | 415,070 |
| 1387 | General tools and implements | 51,358 | 44,979 |
| 1388 | General other equipment | 23,877 | 21,832 |
| | Subtotals | $64,809,107 | $57,935,858 |
| | Preliminary and organization expense | 480,008 | 480,008 |
| | Engineering and superintendence during construction | 3,218,585 | 2,881,000 |
| | Administration and legal expense during construction | 340,094 | 304,084 |
| | [fol. 175] | | |
| | Taxes during construction | 875,171 | 778,044 |
| | Interest during construction | 4,351,934 | 3,883,282 |
| | Miscellaneous construction expenditures | 680,187 | 608,169 |
| | Cost of financing | | |
| | Working capital | 775,000 | 775,000 |
| | Materials and supplies | 509,400 | 509,400 |
| | Going-concern value | 2,000,000 | 2,000,000 |
| | Totals | $78,052,486 | $70,176,845 |
| | Gas leases | 2,874,390 | 2,874,390 |
| | Grand totals | $80,926,876 | $73,051,235 |

## Annual Depreciation and Depletion Requirements

The respondents claim a total of $3,276,325.07 as an allowance for annual depreciation and depletion requirements. Of this amount $2,183,555 was claimed as the necessary allowance for physical equipment other than gas leases. An amount of $1,092,770.07 was claimed as a necessary allowance for annual reserve requirements pertaining to gas leases.

## Requirements for Physical Equipment Other Than Gas Leases

Exhibit 27 sets forth the amounts claimed for annual depreciation covering each classification of physical property. By comparing these amounts with the cost to reproduce new the physical property as set forth in Mr. Hamilton's exhibit, we have found the annual percentages as applies to each classification of property as claimed by the company are as follows:

| | | Per cent |
|---|---|---|
| Production | field measuring stations | 9.36 |
| Production | other structures and equipment | 5.43 |
| Production | gas well construction and equipment | 6.25 |
| Production | field line equipment | 7.25 |
| Production | drilling and cleaning equipment | 10.00 |
| Transmission | rights of way | 2.47 |
| Transmission | other structures | 3.71 |
| Transmission | measuring stations | 3.39 |
| Transmission | compressing station structures | 3.09 |
| Transmission | compressing station equipment | 2.90 |
| Transmission | line equipment | 2.35 |
| Transmission | other equipment | 5.00 |
| General | other structures | 6.71 |
| General | office equipment | |
| General | store equipment | |
| General | shop equipment | |
| General | stable equipment | |
| General | laboratory equipment | |
| General | tools and implements | |
| General | other equipment | |
| Average, per cent | | 3.01 |

It will be noted that these percentage allowances range from 2.35 per cent to 10 per cent. 2.35 per cent is the allow- [fol. 176] ance claimed for the pipe line and this figure is supported by the testimony that some of the main pipe lines have a life of over fifty years and are extended into the Amarillo field, which has a sufficient reserve to supply the lines for a period equal to their lives.

The percentage allowances as claimed by the respondents are not disputed by the evidence. We have accepted such percentages and applied them to the present cost of reproduction as found by us. By applying these percentages to the values which we find, we have calculated that the annual allowance for depreciation of physical property would be $1,894,022, based on physical property values at September 1, 1931.

However, the value of the physical property at September 1, 1931, is not a basis for the measure of depreciation during the years ended December 31, 1930, and June 30, 1931. As is pointed out in the discussion herein relating to the rate base and the average values which should be included in the rate base for comparison with the return earned during a stated period, the annual allowance for depreciation should be based upon the average value of the physical properties during the earning periods under consideration.

In this instance the annual allowance for depreciation should be based on the average value during the year ended December 31, 1930, and the average value during the year ended June 30, 1931, calculation of which is hereinafter set out.

We have applied the annual rates for depreciation, set forth above, to the physical property values which we have adopted herein as at September 1, 1931, and have found the weighted average rate of 2.96 per cent. Applying this percentage to the average value of physical properties for the year ended December 31, 1930, we find the depreciation allowance for that year should be $1,693,312, and in like manner have found the depreciation allowance for the year ended June 30, 1931, to be $1,712,216, which gives us an average depreciation allowance for the two-year period covered by the investigation of $1,702,764.

## Requirements Pertaining to Gas Leases

The respondents claim an allowance for annual reserve requirements pertaining to gas leases as follows:

| | |
|---|---|
| General development expenses capitalized | $532,530.77 |
| Amortization of nonproducing leases | 314,981.68 |
| Dry-hole expense | 174,747.74 |
| Depletion of producing leases | 70,509.88 |
| Total | $1,092,770.07 |

These will be discussed in their order.

[fol. 177] General Development Expense—Capitalized

The company asks for a reserve allowance of $532,530 for general development expense capitalized.

Mr. Eastman testified that this item includes the following character of expenditures:

Cost of acquiring leases.
Geological expense.
Lease rentals.

The cost of acquiring leases was made up of salaries and expense of men engaged in acquiring leases and scouting expenses.

The item of $532,530 represents the expenditures for leasehold development charged to capital investment during 1930. These general development expenses are capitalized and also charged off through the reserve during the same year. The result would be the same if these expenditures were charged directly to an expense account. The general development expenses are not charged off each year on the books. Some rentals paid on leases sold to the Texoma Company are included in this amount.

The practice of the company is to charge expenditures for general development to fixed capital currently as such expenditures are made. Then, annually, the aggregate of such expenditures during the year are charged to expenses and included in expenses for that year, and the same amount credited or added to the reserve for depreciation and depletion. Under this practice the general development expenses are not charged off on the books each year,

but are accumulated from year to year in fixed capital account and if the company followed this practice consistently, a like accumulation would be made in the depreciation and depletion reserve.

The effect of this practice is to include in expense each year the total development expenses and also to include them in fixed capital accounts, the latter being offset by the reserve for depreciation and depletion.

The cost of acquiring leases, including geological and scouting expenses, are capital expenditures. They go to make up the present value of the leases upon which a return is allowed. When a field starts producing, the items mentioned above are part of the value of the lease which is charged off during its producing life and return of capital is provided for under the allowance for "depletion of producing leases." If the cost of acquisition and other expenses enumerated above are included in the annual allowance for depletion, and if in addition a return is allowed on the value of the leases, which includes these expendi- [fol. 178] tures, there would then be a duplication of charges. That is, the expenditures would be included in expenses in the first instance and included in the rate base for a return in the latter.

The value of the leases as found by the Commission is the present fair value which includes among other elements, the cost of acquisition, scouting, and geological expense, and to include such expenditures in an allowance for annual depletion would result in returning the company its investment the same year the expenditure was made while including it in the rate base for the purpose of a return.

We conclude, therefore, that all the items which make up the $532,530, with the exception of annual lease rentals, are a duplication and should be excluded from the annual allowance for depletion as it is covered by the present value of the leases and so included in the rate base. All of this item, with the exception of annual lease rentals, should also be excluded for the reason that the evidence shows that the undeveloped gas reserves assigned to the company consists of 28,970 acres of leases, all of which except 1,060 probable are proven and which, therefore, will not require any development such as scouting, geological investigation and the other expenses going to make up this item.

An allowance for annual lease rentals presents a much more difficult question. It is doubtful whether or not any such allowance should be made. The matter was covered in Re United Fuel Gas Company, P. U. R. 1924A, 357, 366, where it was said:

"There never was and there is not now any good reason why the consumer should pay the royalties and delay rentals. The royalties and delay rentals are for the purpose of carrying the investment of the company in its gas. The gas belongs to the company and it should take care of the royalties and delay rentals in the same manner as it would take care of the interest on its bonded indebtedness. The delay rentals are for the purpose, as stated above, of extending the life of the undeveloped leases. The company may take such leases and surrender them at will and the consumer has no remedy against such conduct on the part of the company. If the consumers have no rights in the premises, they should not be compelled to furnish a fund with which the company may gamble at will. The question of taking, carrying and surrendering gas leases is one that appeals direct to the sound discretion of the managing officials of a gas company and their responsibility should be impressed upon them by compelling the company, and not the consumers, to pay these delay rentals."

Because we have included 1,060 acres of gas reserves in Kansas and Oklahoma, as used and useful, due to their ad-
[fol. 479] vantageous location, we are inclined to make an allowance sufficient to cover lease rentals on such acreage.

We have found 71,276 acres of leases of which 28,970 acres are now developed or producing to be used and useful. No rentals are paid on producing leases. 27,910 acres of the undeveloped leases are located in the Amarillo proven sweet gas field and the remainder, amounting to 1,060 acres, are situated in Kansas and Oklahoma. The undeveloped leases which are assigned to the company and which are situated in the Amarillo field, and which are undeveloped, are in a block acreage, and are in what is known as the Burnett lease on which an annual guaranteed royalty of $50,000 a year is required to be paid, in lieu of annual rental, which annual guaranteed royalty is charged by the company as an expense of operation. For this reason, no additional

allowance should be made to the company for rental on these leases. This leaves 1,060 acres in Kansas and Oklahoma which are undeveloped and on which a rental will be required to be paid. There is no evidence in the record showing exactly the amount of rental which must be paid to hold these undeveloped leases in Kansas and Oklahoma, but as in general the leases which have been introduced in evidence show that the rental which is required to be paid until development is made is, in no case, more than $1 per acre per year, we assume that the rental on these leases is that amount and we, therefore, allow for annual rental on these leases the sum of $1,060. This $1,060 we find is the only amount which should be allowed for this account.

### Amortization of Nonproducing Leases

The company seeks to include in its annual reserve allowance an amount of $314,981.68 for the amortization of nonproducing leases.

Mr. Eastman testified that the amount claimed for amortization of nonproducing leases is to provide a reserve to amortize the cost of leases which are nonproducing:

The amount amortized is the purchase price or bonus paid for leases.

For example, in the case of ten-year leases, one-tenth of the purchase price is to be charged to expense each year until the expiration of the lease or until a well is drilled, to amortize its cost over the period of the term of the lease, or over the period of ten years.

The figure of $314,981.68 is taken from the books and covers the year 1930.

The company thus seeks to have included in expenses as [fol. 180] an annual reserve allowance, the cost of leases through the amortization charge, and also asks to have the present fair value of the leases included in the rate base on which to earn a return.

The present fair value of these leases is included in the valuation of the company's property and in the rate base on which these leases will be allowed a return. This value covers not only all the actual costs, including the bonus paid for the leases, but also the additional enhancement in value caused by their appreciation in value as of September 1, 1931. This, in most instances, is many times the actual cost of the lease.

There is, in fact, no depreciation or depletion of an undeveloped lease until it has been drilled and commences to produce gas. As soon as a lease becomes productive annual expense for depletion is allowed and provided under amortization of producing leases. In the meantime the company is allowed a return on not only the cost, but on the full, fair value of the lease, and it is seen, therefore, by this contention the company is asking to have returned both the cost of the leases through an annual reserve charge and also return on the fair market value of the leases, and when the leases become productive to have the full value of the developed leases returned through amortization of producing leases.

If a return is allowed on the fair market value of these undeveloped leases, which includes the bonus paid, we believe that no reserve allowance should be made so long as they are nonproductive.

If the company were allowed one-tenth of the value of these leases annually for ten years it would thus have returned to it in that time the fair value of these leases, amounting to $1,169,500, irrespective of whether the leases were producing, and thus the present consumers would be required to pay for the amortization of these leases although they would have received no gas and no benefit from them. We believe that if the consumers are required to pay a rate for gas based on a return upon the fair value of its properties, including the fair value of these leases, they should not be required also to pay for the amortization of nonproductive leases which are not, in fact, being depleted.

If and when the nonproducing leases expire or are surrendered because they have been found to be nonproductive, then and not until then, is the time when their cost or value should be charged as an expense, and if the lease through development becomes productive, annual depletion is then allowed in the item of depletion of producing leases.

[fol. 181] Even if the contention of the company that it should be allowed an annual expense for amortization of nonproducing leases were conceded to be sound, amortization of such leases based upon the experience of the company for the year 1930 is not a fair measurement of annual

requirement for amortization in future years, commencing with September 1, 1931. This is for the reason that on the findings herein made the company will have as used and useful leases, as of September 1, 1931, only 28,980 of undeveloped leases, valued at $1,460,500, while the company's estimate of $314,981.68 claimed for annual depreciation is based on holdings of approximately 1,220,064 acres of undeveloped leases held by it in 1930, valued by it at over $10,000,000.

In the allowance to the company for nondeveloped leases which are used and useful, as herein found, there are 27,910 acres which are conceded to be proven and only 1,060 acres are classified as probable, and it is improbable that any of these leases will be surrendered or permitted to expire.

We find that there should be no allowance for this account.

### Dry-hole Expense

The respondents ask for an annual allowance or reserve in the amount of $174,747.74 for dry-hole expense. This figure is based upon the experience of the company for the year 1930. During the period 1929 and 1930 many new prospective gas fields had been discovered, and the company was acquiring new leases and proving them by actual development. Many of these prospective gas fields were a considerable distance from the pipe line of the company.

During the year 1930 the company drilled ten dry holes on scattered acreage in Oklahoma, Kansas, and one well in Texas, none of which was drilled in the territory now designated as proven area. The testimony before the Commission clearly discloses that the pioneering period is past. The company now has sufficient developed and proven acreage to satisfy all its requirements for many years. The testimony of both the respondents' and the Commission's witnesses is to the effect that in this proven area there is little or no likelihood of encountering a dry hole in the development of this proven territory. (In fact the valuation upon these leases is fixed and based on the supposition of these leases being proven.) It is true that the company does have unproven and undeveloped acreage, but this acreage is in excess of any reasonable reserve which the company need carry for the protection of its consumers

[fol. 182] and is in excess of any reasonable reserve which should be included in the rate base.

We believe that it would be unsound to use a figure based on the experience of the company during a period when it was pioneering in gas discovery and gas development, in territory which we find is not now used or useful for the purpose of supplying its customers. This is supported by the testimony that the company is now abandoning leases, and has during the period covered by this investigation, sold a large block of its acreage which indicated that part of its acreage was obtained in excess of its reserve requirements and for speculative purposes.

Although there was no testimony that there were any dry holes drilled in the year 1931, and although the testimony of all the witnesses disclosed that there is little likelihood of dry holes being encountered in the proven reserves, herein assigned to the company as used and useful, nevertheless, we deem it advisable to make a reasonable allowance for dry-hole expense.

The evidence shows that the cost of drilling a dry hole varies from $3,000 to $21,000 depending upon the area in which the well is drilled. We believed that an allowance of one dry hole per year, based upon an average of these two figures, would be an ample allowance for this account. We therefore find an allowance of $12,000 to be reasonable.

Annual Requirements for Depletion of Producing Leases

The respondents asked for an annual allowance of $70,569.88 for depletion of producing leases.

The company has arrived at this figure by using the estimated life of the various fields, and the rate at which they are being depleted. We find this to be a reasonable allowance.

We, therefore, find the reasonable allowance for annual reserve requirements pertaining to gas leases to be $83,569. This total added to the average annual depreciation and depletion requirements pertaining to physical equipment other than gas leases in the amount of $1,702,764, gives a total requirement of $1,786,333, which we find to be a reasonable average annual allowance for the periods covered by this investigation.

[fol. 183] Net Earnings of Company Available for Annual Return and the Return Earned

Average Value During Period Covered by Earning Statement

The valuation of the properties of the pipe-line companies were made on behalf of both the companies and the engineering department of the Commission as of September 1, 1931. There should be included in the valuations only properties used and useful in rendering service.

The exhibits introduced relating to income and expenses and net income for the purpose of comparing such net income with the value to determine the rate of return being earned cover principally the calendar year 1930 and the twelve months' period ending June 30, 1931. About the close of the hearing, the company introduced exhibit 92, consisting of one single typewritten sheet which purported to show the net income during the calendar year 1931.

It is obvious that a comparison of net income during 1930 with the value of property used and useful as of September 1, 1931, would furnish no indication of the net return earned during 1930 on the value of the property used and useful during that year, as large additions were made to the property currently during all of that period as well as during the period from December 31, 1930, to September 1, 1931. It must be presumed that additions to the properties were made for the purpose of securing additional revenue or bringing about economies in expenses.

In determining the return earned on property used and useful during 1930, the value of the property used and useful during that period must be found. The only evidence from which such finding may be made consists of the value at September 1, 1931, as testified to by the engineers, and the cost of the net additions from January 1, 1930, to September 1, 1931, as shown by the books and records of the company. In the absence of any very radical change in price levels during the period mentioned, the actual cost of the net additions should compare with the value of such additions at September 1, 1931. Therefore the value of the property used and useful during 1930, which produced the net income earned during 1930, may be fairly ascertained by deducting from the value at September 1, 1931,

the net additions from January 1, 1930, to September 1, 1931, and adding thereto the average additions during the year 1930.

The average additions should be given consideration because obviously additions made during December, 1930, [fol. 184] are not related to earnings during January, 1930, and the additions made during December should be included for one-twelfth of the year, while the additions made in January should be included for twelve-twelfths of a year and the same principle applied to additions during other months.

The cost of reproduction new, exclusive of gas leases, at September 1, 1931, as found herein, is $78,052,486. The cost of reproduction new during the annual periods ending December 31, 1930, and June 30, 1931, has been estimated as follows:

| | |
|---|---|
| Cost of reproduction new September 1, 1931 | $78,052,486 |
| Deduct net additions to fixed capital, July 1, 1931, to September 1, 1931 (Ex. 91) | 1,362,506 |
| Cost of reproduction new July 1, 1931 | $76,689,980 |
| Deduct net additions January 1, 1931, to June 30, 1931 (Ex. 51) | 777,591 |
| Cost of reproduction new January 1, 1931 | $75,890,389 |
| Deduct net additions July 1, 1930, to December 31, 1930 (Ex. 51) | 10,471,653 |
| Cost of reproduction new July 1, 1930 | $65,440,736 |
| Deduct net additions January 1, 1930, to June 30, 1930 (Ex. 51) | 592,021 |
| Cost of reproduction new January 1, 1930 | $64,848,715 |

Applying the same per cent condition (89.94) as we found at September 1, 1931, to each of the above reproduction costs results in the following cost of reproduction new less depreciation:

| | |
|---|---|
| September 1, 1931 | $70,199,323 |
| July 1, 1931 | 68,977,181 |
| January 1, 1931 | 68,277,816 |
| July 1, 1930 | 58,859,611 |
| January 1, 1930 | 58,327,147 |

The average values found by adding the values at the beginning and end of each period and dividing this total by two follow:

| | |
|---|---|
| Year ended December 31, 1930 | $63,302,482 |
| Year ended June 30, 1931 | 63,918,396 |

To which should be added $2,874,390 for the value of the gas leases, which results in average rate bases for the periods of—

| | |
|---|---|
| Year ended December 31, 1930 | $66,176,872 |
| Year ended June 30, 1931 | 66,792,786 |

Reducing these values to an average figure, we find the average value for the periods covered by the investigation to be $66,484,829.

## Net Income

For the purpose of arriving at the pipe line company's income two annual periods were used in the investigation.

The net income resulting from the operations of the pipe line system during two annual periods ended December 31, [fol. 185] 1931, and June 30, 1931, respectively, follows:

| | 1930 | 1931 |
|---|---|---|
| Net income (Ex. 49, p. 7) before depreciation and depletion | $8,829,480 71 | $8,741,899 14 |
| Add: | | |
| Payments to Henry L. Doherty & Co. at rate of 1¾ per cent | 75,022 33 | 68,882 05 |
| Adjustment of federal income tax accrual credited to surplus (Ex. 49, p. 8) | 23,310 00 | |
| Construction credit (Ex. 92) | 78,874 00 | 78,874 00 |
| Adjusted net income before depreciation and depletion | $9,006,687 04 | $8,889,565 19 |

The item of 1¾ per cent payments and the reasons it should be disallowed as an item of expense are discussed elsewhere herein.

The adjustment of federal income tax accrual represents a reduction of taxes as stated in expenses.

This adjustment represents the amount charged to expense in anticipation of the federal income tax over and above the amount actually paid.

The construction credit does not appear in the statement of income and expenses covering the periods ended December 31, 1930, and June 30, 1931, but it is shown on ex-

hibit 92, which purports to set forth the expenses during the year ended December 31, 1931. This item of $78,874 represents a reduction in expenses and a like addition to fixed capital representing a proportion of expenses due to construction activities. Those items which appear in expenses include general and administrative expenses, such as salaries and expenses of officials and office employees, legal expenses, rent and some general development expenses, which were charged currently to expenses. At the end of 1931, it appears that a portion of such expenses were found to be attributed to construction activities and portions so found added to fixed capital accounts and expenses correspondingly reduced. The manner in which the amount of expenses charged to fixed capital accounts was determined does not appear in the record. No similar adjustments appears during the periods ended December 31, 1930, and June 30, 1931, and as a large amount of construction was carried on during those periods allowances should be made by reducing expenses, just as they were reduced on exhibit 92. No testimony appearing as to the exact amount which should be deducted it is reasonable to presume that the construction credit should at least equal the credit during 1931; and we have therefore made such adjustment in arriving at net income above.

By averaging the adjusted net income before depreciation and depletion for the two annual periods, December 31, 1930, and June 30, 1931, we find an average annual income of $8,948,126.11 for the periods covered by the investigation. Deducting from this amount the allowance for depreciation, depletion and lease rentals in the amount of [fol. 186] $1,786,333, we find the average annual net income of the company available for return in the amount of $7,161,793, during the periods covered by the investigation.

## Average Return Earned During Annual Periods Covered By Investigation

At the beginning of this investigation, the Commission directed that income during at least two annual periods be included in order to eliminate any abnormal fluctuations which might occur and to get a better picture of the average business conditions of the company affecting the gate rate contract. It is the belief of the Commission that rates

should be based on contemplated average conditions over a reasonable period of time. The Commission realizes that the reasonableness of the contract should not be affected and that the contract should not be changed with every minor change in values and costs and minor fluctuation in business conditions.

At the suggestion of the company, the two periods used was the year ending December 31, 1930, and the annual period ending June 30, 1931. The Commission has, therefore, based all its findings on the average of those two periods.

Counsel for the respondents in their reply brief, suggest that the Commission should disregard these periods, or as they state, not "hold the company to the experience of prosperous years."

It appears to be their contention that the Commission should be guided largely by decreased earnings set out in their reply brief which have occurred since the hearing closed. This we do not believe to be proper. The Commission realizes that it is fixing rates for the future and not for the past, but it does not believe that it should be influenced too greatly by decreased earnings occurring over a short period, which can hardly be expected to last indefinitely into the future. In fixing a rate for the future based on past and present conditions, the Commission believes it should give consideration to the present decrease in earnings, and such decrease will be recognized in our conclusion and adjustment of the contract.

From our previous calculations, we have found a present average value of the pipe-line property over two annual periods covered by the investigation to be $66,484,829. We have found the average net income of the company available for return during the same periods to be $7,161,793. This gives an average return earned during the annual periods covered by the investigation of 10.77 per cent.

The Commission is of the opinion that a net return of [fol. 187] approximately 11 per cent is unreasonable at the present time, and was unreasonable during the periods covered by the investigation. It is the opinion of the Commission that no company, dealing at arm's length with an independent company should expect to enter into a contract under conditions such as existed during 1930 and 1931, or up to the present time, by which they would make a net return of 10.77 per cent in a gas pipe-line business.

The Commission appreciates the fact that it is not fixing a definite rate, but in so far as the reasonableness of this contract is to be tested by what it costs the pipe line company to render service, and the rate of return earned, it will be necessary for the Commission to find what is a reasonable return for the pipe line company under present conditions by which to test the reasonableness of the contract.

## Fair Rate of Return

In considering what is a fair rate of return to be earned by the pipe line company as a test of the reasonableness of the gate rate contract, the Commission has necessarily taken into consideration what the utility must earn in the light of its situation, its requirements and its opportunities. In dealing with its affiliated distributing companies the Commission has considered the fact that the company should be allowed to earn on the value of its property employed in serving the public with its pipe line, an amount equal to that generally being made by the same business undertakings, which are attended by the same risks and uncertainties. The Commission has also given consideration to the fact that the utilities should be allowed to earn an amount reasonably sufficient to assure confidence in its financial ability and has also considered the amount of risk involved in the pipe line business.

Witness for the respondents testified that an eight per cent return is the usual allowance for public utilities. Other testimony placed the rate of return from six to eight per cent. Practically all of the witnesses agreed that some consideration should be given to the fact that this company was not an ordinary public utility company, but one of a part of a large system organized for the purpose of maintaining the credit of the constituent companies and securing financial assistance. As to just what reduction should be made in the rate of return because of this factor was not stated. To this testimony the Commission must give its own independent consideration in connection with the principles laid down above.

[fol. 188] The testimony was to the effect that because of the assistance of the holding company, the Cities Service Company, the Cities Service Gas Company is and has been able to sell its securities at an "interest rate that was from a half to three-fourths per cent less than anything else that

was put out at about that time on a similar project," and in addition that it gets better terms on its mortgages. It does not have to pay them off in ten years as many of the pipe-line companies have had to do with issues that have been put out in the last two years. Because of this, the Cities Service Gas Company was able to sell its 5½ per cent bonds for 96¼.

"The company having ample financial resources does not necessarily have to issue securities now or six months from now or two years from now. They pick and choose their time when the markets are right."

Page 30, exhibit 49, shows that the company actually sold twelve million dollars of first mortgage, pipe line six per cent gold bonds of the Cities Service Gas Pipe Line Company at par.

It would, therefore, appear that the company is able to obtain funds at a very low rate and is assured of financial stability and a supported credit which enables it to raise the money for the proper discharge of its duties at a very low rate of interest.

It would also appear from the record that there is little risk or hazard in the business of the Cities Service Gas Company. The pipe-line system which it has established is a permanent fixture for an indefinite period. It has a gas reserve which insures it of a supply of gas lasting well into the future. The territory which it serves is well protected; the company has almost a monopoly on the territory which it serves due to the fact that the distributing units are interrelated companies and it would be economically unsound for another pipe-line company to invade its territory.

We are also confronted with changed conditions affecting opportunities for investments which tends to limit the amount of the return. Annual returns upon capital have materially decreased in the past years. Businesses generally are satisfied with a very low rate of return. All businesses, including that of public utilities, are satisfied with a much less rate of return than they were four or five years ago when annual returns upon capital were unreasonably high. Regulatory bodies and courts generally have recognized this factor.

The Cities Service Gas Company is not an ordinary pub- {fol. 189} lic utility, but one of a large system organized

for the purpose of maintaining the credit of subsidiary companies and assisting them in their finances. The records of the Cities Service Gas Company show that it has been able to expand its business so as to meet increased demands, to pay its operating expenses, including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and accumulate a large surplus. These factors were recognized as material in determining the rate of return in the recent case of Smith v. Illinois Bell Telephone Company, 282 U. S. 159, 191, in which the court said:

"It is evident that in the present case we are not dealing with an ordinary public utility company, but with one that is part of a large system organized for the purpose of maintaining the credit of the constituent companies and securing their efficient and economical management. The record of the Illinois company shows that for many years it has been able to expand its business so as to meet increasing demands, to pay its operating expenses including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and to accumulate a surplus."

The history of the pipe line under consideration discloses that its operations have been highly successful and enormously profitable. The Cities Service Gas Company was organized in the latter part of 1926, acquiring the assets and assuming liabilities of the following companies:

Empire Natural Gas Company.
Kansas Natural Gas Company.
Empire Gas and Pipe Line Company.
Kansas Oklahoma Gas Company.
Empire Gas and Fuel Company (Delaware). (Gas properties only.)

The stock control of these companies had been theretofore acquired by the Cities Service Company and their assets were acquired and liabilities assumed by the Cities Service Gas Company as of November 30, 1926.

The history of these pipe line companies is a matter of common knowledge and the Commission is familiar with their financial and other operations during the past approximately twenty years. Some of them, if not all, had been in receivership; they had been before the Commission many

times and the Commission had, about 1922 or 1923, acquiesced in the installation of the 40-cent gate rate. The 40-cent gate rate was fixed because it was represented that the companies had been operating at a loss and that there was [fol. 190] an insufficient gas supply.

The effect of the 40-cent gate rate on the financial results of the companies is very clearly illustrated on pages 24 and 25 of Montgomery's exhibit 49. On these pages are set out balance sheets as of November 30, 1926, of the above-named companies, which were consolidated into the Cities Service Gas Company as of November 30, 1926.

These balance sheets show that at the date indicated the book value of the plant investment of the companies, including uncompleted job orders, was $52,182,525.98, and that reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95. These reserves which had been accumulated out of earnings amounted to 42.97 per cent of the plant investment.

These balance sheets further show, notwithstanding the fact that only a few years prior to November 30, 1926, the companies had represented that they had been operating at a loss and proceeded to increase their gate rates to 40 cents, that they had accumulated surplus amounting to $14,903,660.21, which sum is equal to 87.26 per cent of the total capital stock of the companies taken over.

The combined reserves for depreciation and depletion and surplus amounted to $37,327,597.16, which is equal to 218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment.

In the case of the Empire Natural Gas Company, it had a capital stock of $10,574,000, and compared to such capital stock it had surplus of $6,066,436 and reserves for depreciation and depletion of $10,192,715, a total surplus and reserves of $16,259,151, which is equal to 153.77 per cent of its capital stock.

The plant investment of the Empire Natural Gas Company, including uncompleted job orders, as reflected in the books of the company as of November 30, 1926, was $26,577,355; its reserves for depreciation and depletion amounted to $10,192,715, which is equal to 38.35 per cent of the plant investment.

In the case of the Kansas Natural Gas Company it had a capital stock of $6,000,000 and surplus of $7,784,067 and

had accumulated reserves for depreciation and depletion amounting to $11,905,381. Its surplus amounted to 129.73 per cent of its capital stock and the combined surplus and reserves amounted to 198.42 per cent of its capital stock. [fol. 191] The book value of its plant investment was $18,861,223, including uncompleted job orders, and its reserves for depreciation and depletion of $11,905,381 was 63.12 per cent of such plant investment.

The Empire Gas and Pipe Line Company had a capital stock of $5,000 and surplus of $907,323 which was 18,146.46 per cent of its capital stock. Its reserves for depreciation and depletion was $325,840, making the combined reserves and surplus $1,233,163, all of which was accumulated on a capital stock of $5,000.

The plant investment of the Empire Gas and Pipe Line Company, including uncompleted job orders, was $1,625,569 compared with combined surplus and reserves of $1,233,163.

These companies were so prosperous under the 40-cent gate rate during these few years that they were able to loan money to other affiliated companies to the extent of $7,569,571, in addition to paying bond interest and dividends.

Page 23 of exhibit 49 shows what happened when the Cities Service Gas Company was organized and its books opened: $17,080,000 of capital stock and $2,000,000 of bonds became immediately $25,000,000 of common stock and $25,000,000 of 5½ per cent bonds; its reserves for depreciation and depletion became $7,760,706 instead of $22,423,936, as they were before the consolidation. No surplus was carried over into the new Cities Service Gas Company.

The financial history of the company since the consolidation in November, 1926, may be found on pages 1 to 8, inclusive, in exhibit 49, which reflects the combined operations of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company and the American Pipe Line Company.

It is shown there that surplus has been accumulated, in excess of all interest and dividends paid, of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have increased to $10,818,020. Its total assets have increased from $60,595,001 as of December 31, 1926, to $109,431,039 as of June 30, 1931. This enormous increase was accomplished with the addition to the outstanding stock and bonds of only $28,365,700 and loans of $9,000,000. The

company has prospered so that it was able to advance to affiliated companies $2,677,134.

The Cities Service Gas Company has during all this time paid interest on its bonds and dividends on its capital stock; in 1928 it paid $1,000,000 dividends and in 1929 and 1930 it paid $2,000,000 each on dividends, which is at the rate of 8 [fol. 192] per cent per annum. Its earnings before interest were as follows:

| | |
|---|---|
| 1927 | $5,385,739 |
| 1928 | 6,053,621 |
| 1929 | 8,060,793 |
| 1930 | 8,829,480 |
| Twelve months ending June 30, 1931 | 8,741,809 |

The net profit of the companies, after paying all interest charges, available for reserves and common stock during each of the years 1927 to 1930, was:

| | | | |
|---|---|---|---|
| 1927 | 14.99% | 1929 | 21.25% |
| 1928 | 13.12% | 1930 | 19.97% |

Its net profit after paying all interest and other charges providing for substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

| | | | |
|---|---|---|---|
| 1927 | 9.96% | 1929 | 14.53% |
| 1928 | 6.75% | 1930 | 10.82% |

Page 1 of exhibit 49 shows that the plant investment, including uncompleted job orders, increased from $54,243,128 as of December 31, 1926, to $99,003,996 as of June 30, 1931, an increase of $45,760,872. During this period a large line was constructed from Amarillo to Wichita; a line was extended from in the neighborhood of Hutchinson north into Nebraska; lines were extended into Missouri and a great program of expansion carried out. Such program involves large expenditures which affect the operating expenses of the company.

Further, as pipe-line extensions were developed, they necessarily were not fully productive until the volume of sales had been built up to the capacity of such extension. A large proportion of the investment each year was unproductive, although the investment has been included in the

plant investment values included in the above, and will be included in the future. This discussion relative to idle plant is merely for the purpose of illustrating that the company has been earning a high return not only on its production property but on its idle and unproductive property.

During times of higher price levels and when the purchasing power of the dollar was very much less than it is at the present time, eight per cent was generally considered a fair and reasonable rate of return.

The present low level of prices is a matter of common knowledge and the purchasing power of a return of six per [fol. 1931] cent is now greater than the purchasing power of a return of eight per cent was during the periods of higher price levels.

A return of six per cent would not be unreasonable at this time. In fact, the great majority of concerns doing business now are fortunate if they earn as much as six per cent.

We believe that in view of the financial history of this pipe line system, its highly profitable experience, the fact that it is part of a large system with its market assured through affiliated distributing companies, its enormous gas reserves, and all surrounding circumstances, that the maximum rate of return which the Commission should use in determining the reasonableness of the contract is 7 per cent.

System Earning in Excess of a Fair Rate of Return of 7 per Cent During the Annual Periods Covered by the Investigation

The average net income of the company, available for return, during the periods covered by the investigation was $7,161,793, and the average fair value for the same period was $66,484,829. A fair return on the average value at the rate of 7 per cent per annum is $4,653,938, which compared with the net income of $7,161,793 is $2,507,855, in excess of a fair return of 7 per cent.

The gas sold by the company is classified by it as follows:

Domestic:
Main line.
Town-border main line.
Town-border local fields.

Industrial:
Maine line.
Town-border main line.
Town-border local fields.
Drilling and field gas.
Sales to other pipe-line companies.

Main line domestic gas is gas sold from the main line direct to domestic customers.

Town-border main line domestic gas is gas sold from the main line to distributing companies for resale for domestic consumption and these sales are the subject of this investigation.

Town-border local fields gas is gas sold from local fields to nearby distributing companies for resale.

[fol. 194] Industrial gas is gas sold for manufacturing and industrial purposes.

Drilling and field gas is sold in the gas fields for drilling and other purposes.

Sales to other pipe-line companies represents sales to other pipe-line companies who in turn resell it.

The average rates per M. c. f. received from gas sales follows:

| Domestic: | 1930 | 1931 |
|---|---|---|
| Main line | 47.2¢ | 47.0¢ |
| Town-border main line | 39.5¢ | 39.5¢ |
| Town-border local fields | 19.3¢ | 17.3¢ |
| Industrial | 15.6¢ | 15.4¢ |
| Drilling and field gas | 18.6¢ | 18.0¢ |
| Sales to other pipe-line companies | 8.4¢ | 7.4¢ |
| Average (weighted) | 23.2¢ | 23.9¢ |

Any reduction made as a result of this investigation would affect only the sales of domestic gas from main-line town-border stations.

The sales of domestic gas from main-line town-border stations during 1930 totaled 20,331,209 M. c. f., at the average price of 39.5 cents per M. c. f., producing a total revenue of $8,032,923.

The sale of domestic gas from main-line town-border stations during the annual period ended June 30, 1931, totaled 21,442,841 M. c. f., at the average price of 39.5 cents per M. c. f., producing a total revenue of $8,484,311. The aver-

age annual revenue from main-line town-border domestic gas sales for the periods covered by the investigation was $8,258,617.

The average annual net income from all operations during the periods covered by this investigation, if these domestic sales had been at 30 cents, 32 cents and 35 cents, respectively, would have been as follows:

| | |
|---|---|
| 29½-cent rate | $5,066,848 |
| 30-cent rate | 5,171,283 |
| 32-cent rate | 5,589,025 |
| 35-cent rate | 6,215,634 |

The Commission, however, appreciates the fact that some consideration must be given to present conditions, which have caused some decrease in the earnings of the company. The Commission also appreciated the fact that it is not fixing a definite rate for the pipe line, but merely using it as a measure to test the reasonableness of the contract.

It therefore appears that if the gate rate were reduced to 29.5 cents, the company would still be making $407,910 in excess of a fair rate of return of 7 per cent on the average value of the property during the periods covered by the investigation.

[fol. 195] The Commission finds that 29.5 cents is a fair and reasonable price to be charged for domestic gas at main-line town-border stations and that anything in excess of 29.5 cents is unreasonable and is not such a contract as parties dealing at arms length under present conditions would enter into.

A 29.5 cent rate for domestic gas for main-line town-border stations results in an average reduction for such gas of 19 cents per M. c. f. A 29.5 cent rate results in an average net income of $407,910 in excess of 7 per cent, which would give the respondents approximately 8 per cent return on the fair value found herein.

At the close of the hearing respondents introduced exhibit 92, which purported to show the loss in earnings after the period covered by the investigation. Although as previously stated, the Commission does not believe that it should test the reasonableness of this contract by an abnormal earning period, but rather on an average period, under average conditions, the Commission realizes that it is de-

termining the reasonableness of the contract for the future and what future conditions may be is somewhat difficult to determine. In view of these conditions the Commission considers that an allowance of a 29.5 cent contract which carries an earning in excess of 7 per cent is liberal.

In their reply brief respondents state that the gross earnings during the first five months of 1932 were several hundred thousand dollars less than the gross earnings for the same period during 1931. Counsel for the Commission suggest that this matter should not be considered as it was not in the record. The Commission feels that they have a general knowledge of the decrease in earnings of all public utilities due to the present depressed condition and that this has been considered by the Commission. In giving consideration to this matter, however, the Commission must also give consideration to other facts of which it has common knowledge. Namely, that the expense of the company has materially decreased with the decrease in gross earnings. The expense of production and transportation of gas is necessarily a big item. In addition, values of all properties have materially decreased. The respondents, in fact, in their last brief, call attention to the fact that salaries and wages of all employees have been recently reduced. It is common knowledge of the Commission that the cost of gas in the fields has been reduced during the past six months. Therefore, decrease in earnings is offset by reduction — expenses.

[fol. 196] Since the beginning of this investigation voluntary reductions in rates have been made at Cherryvale, Newton and El Dorado. Records on file with this Commission, including the orders of the Commission approving the rates, show reductions in the three towns:

Cherryvale on November 5, 1931, was given a new rate of $2.25 for the first 5 M. c. f. as against a previous rate of $3.37 for the first 5 M. c. f., making a reduction of $1.12 for the first 5 M. c. f.

Newton on December 1, 1931, was given a new rate of $3.00 for the first 5 M. c. f., as against a previous rate of $4.75 for the first 5 M. c. f., making a reduction of $1.75 for the first 5 M. c. f.

El Dorado on June 1, 1932, was given a new rate of $2.60 for the first 5 M. c. f., making a reduction of $1.25 for the first 5 M. c. f.

To what extent these reductions affected the earnings of the pipe-line company is not disclosed, but if any reduction in rates were made by the pipe-line company to the operating unit, an order of the Commission reducing the 40-cent charge would not affect the earnings as applied to such sales.

The reduction at El Dorado is of peculiar interest in this investigation, due to the fact that this whole controversy grew out of an attempt to increase the earnings at El Dorado. It is common knowledge that but a short time before the reduction was made at El Dorado the Western Distributing Company, one of the respondents herein, was before the Supreme Court of the United States strenuously contending that the old rate was confiscatory and that the Commission arbitrarily refused to grant an increase of this rate, yet since this contention was made the company has voluntarily reduced their rate.

Respondents in speaking of the decrease in gross earnings in their reply brief, do not disclose whether such decrease is caused by loss in domestic or industrial gas sales: Mr. Montgomery's exhibit 49 shows the revenue from gas sales during the year 1930 and the twelve-months period ended June 30, 1931.

This exhibit shows the domestic sales increased $347,415.85 during the 1931 period compared with 1930, and industrial sales decreased $617,821.98 and field and drilling gas decreased $339,563.58. All of the decrease is in industrial sales and sales other than domestic.

In addition the record shows that the company in 1931 reduced its rate to "other pipe-line companies" from 8.4 cents M. c. f. to 7.4 cents M. c. f., a reduction of over 11 per cent, which indicates that the pipe-line company in dealing with other pipe-line companies recognizes that the cost of producing and delivering gas has decreased.

[fol. 197]

Exhibit 49 further shows that domestic sales increased 686,310 M. c. f. during the 1931 period compared with the 1930 period, and that industrial sales decreased 3,375,194 M. c. f. In so far as the decrease is caused by loss of industrial sales due to temporary abnormal industrial conditions, we do not believe that this additional burden should be placed upon the domestic consumer.

If loss of earnings is due to temporary abnormal industrial conditions it certainly would not be proper to permit

the company to require the domestic business to carry the loss of earnings from the industrial business during the present abnormal period which cannot continue indefinitely into the future. If there is a loss of earnings in this class of business, those rates should be increased to permit that class of business to carry itself.

The Commission also recognizes the fact that the gas company probably has more property in service during the period of 1932 than during the period covered by the investigation. In connection with this, there must also be considered the general decrease in prices which would tend greatly to reduce the valuation of the properties at the present time. To give too serious consideration to these fluctuating conditions would require a reopening of the case and they, no doubt, would be changed before another hearing was completed. The Commission does not believe this to be practical or necessary.

The earnings of 1930 and 1931 were lower as compared to the previous prosperous years, although perhaps not as low as those for 1932, they are no doubt a better measure of the average condition, under which the pipe-line contract must continue. The Commission, therefore, considers in allowing 29.5 cents for town-border main-line gas, that it has reached a fair and equitable result, and that in allowing a return of $407,910 in excess of a 7 per cent return, that they have reached a fair and reasonable conclusion.

## The Gate Rate for Cities in Kansas

We have discussed above the return earned by the company from the operation of its entire system. We are concerned with the rates charged in Kansas.

The pipe-line system is used in delivering gas produced and purchased in Texas, Oklahoma, Kansas and Missouri, to purchasers in those states and in Nebraska. The operations of the system are both interstate and intrastate [fol. 198] in Kansas; gas is received from Texas and Oklahoma into Kansas, and gas is produced and purchased and deliveries are made in Kansas and to the states of Nebraska and Missouri.

A determination of a fair gate rate in Texas requires the determination of the value of property located in Texas

and the expenses incident to the operation of that property and an apportionment of such value and expenses to the cost of gas sold in Texas and to the gas delivered from Texas and other states. The same is true as to the gas produced in Oklahoma, Kansas and Missouri.

By finding the value of the property in Texas and the expenses incident thereto and comparing them with the total gas sold in Texas and delivered from Texas to other states the average cost of gas sold in Texas may be arrived at with some degree of approximation and the remainder of the cost would follow the gas delivered to Kansas.

The Commission, in determining that the reasonable gate rate is 29.5 cents, have used that figure in calculating the effect the reduction would have upon all the earnings of the respondents over its entire system. This was necessary in order to get a fair picture of the entire system, but as a matter of fact, the reduction of 11 cents would only apply to the business in Kansas. It might be that a higher rate would be justified in states further distant from the source of supply. Therefore, while we have figured that the 29.5 cent rate would reduce earnings over the entire system, such would not be true unless the same rate were determined to be reasonable in Nebraska, Missouri, Oklahoma, and perhaps Texas.

It is further found, under the authority of chapter 240 of Laws of 1931, that the costs of this proceeding should be taxed against the respondents.

An appropriate order will be issued in accord with the findings in this opinion.

[fol. 198a] ORDER

Now on this 20th day of July, 1932, the above-entitled matter comes regularly before the Commission for final determination and the Commission finds:

1. That the findings in the opinion on the above-entitled matter filed on the 19th day of July, 1932, should be incorporated in this order and made a part hereof.

2. That the distributing companies, respondents above named and the Cities Service Gas Company are mere agents or instrumentalities of the Cities Service Company.

3. That the contract between Henry L. Doherty and Company and the various distributing companies, respondents above named, under which Henry L. Doherty and Company purports to render various departmental services to the distributing companies, and receives as compensation therefor one and three-fourths per cent of the gross revenues of the distributing companies; an engineering fee of five per cent of the cost of construction; a fee for services of the securities department and an additional expense and per diem charge is unreasonable, and that the compensation received thereunder is excessive to the extent of the payment of the one and three-fourths per cent of the gross revenues of the distributing companies, and is not such a contract as parties dealing at arm's length would enter into.

The Commission further finds:

4. That the contract between the Cities Service Gas Company, a natural gas pipe-line company, respondent above named, under which the Cities Service Gas Company sells gas to the distributing companies at the city gate at an average price of 39.5 per M. c. f. is unreasonable, and that the payments made thereunder are excessive in the amount of ten cents per M. c. f. for such main-line border gas.

5. That 29.5 is a reasonable price to be paid to the Cities Service Gas Company by the respondents for main-line town-border gas, and that any amount paid in excess thereof is unreasonable and is not such a contract as parties dealing at arm's length would enter into.

The Commission further finds:

6. That on and after the 1st day of August, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any pay-
[fol. 198b] ments made to Henry L Doherty and Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payment made to Cities Service Gas Company for main-line town-border gas in excess of 29½ cents per M. c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

The Commission, therefore, further finds:

7. That on and after the 1st day of August, 1932, that because of the reduction in expense item as above mentioned, the rate to the consumer should be reduced in proportion to the reduction in expenses, pending a final determination of the distributing company rates. Such reduction to be measured by the ten-cent reduction per M c. f. and 1¾ per cent of the gross revenue of the distributing company.

8. That on the 1st day of September, 1932, the distributing companies, respondents above named, shall appear before the Public Service Commission at ten o'clock a. m. for the purpose of showing to the Commission cause why such reductions should not be made permanent and cause why other reductions should not be made as the evidence presented might justify.

The Commission further finds:

9. That the budget department of Henry L. Doherty and Company supervises the transfer of cash to and from New York in accordance with the budget estimates of the Cities Service Company, so that the cash which would otherwise accumulate to the distributing companies is sent on to the fiscal agent in New York to be used for operation and construction programs at other centers, contrary to the statutes of the state of Kansas. (R. S. 17-616.)

10. That under the contract between the Gas Service Company and the various distributing companies, respondents above named, under which the Gas Service Company operates and manages the distributing companies and keeps some of their books and charges to such distributing companies certain sums monthly should not be approved by the Commission because the general ledger and other general books of the distributing companies and practically all of the funds of the distributing companies, pending their transfer to New York, are kept in Kansas City, Mo., contrary to the laws of the state of Kansas. (R. S. 17-616.)

It is, therefore, by the Commission ordered:

1. That on and after the 1st day of August, 1932, the distributing companies, respondents above named, shall [fol. 198c] cease to set up on their books as an expense

item any payments made to Henry L. Doherty and Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payments made to Cities Service Gas Company for main line town border gas in excess of twenty-nine and one-half cent per M c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2. That on and after the 1st day of August, 1932, the rate to the consumer shall be reduced by the distributing companies in proportion to the reduction in expenses above named, pending a final determination of the distributing company rates. Such reductions to be measured by the ten-cent reduction per M c. f. and 1¾ per cent of the gross revenue of the distributing companies.

3. That on the 1st day of September, 1932, the distributing companies, respondents above named, shall appear before the Public Service Commission at ten o'clock a. m. for the purpose of showing to the Commission cause why such reductions should not be made permanent and cause why other reductions should not be made as the evidence presented might justify.

By the Commission it is so ordered:

Thurman Hill, Chas. W. Campbell, Commissioners.

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Opinion on rehearing omitted here, being identical with Exhibit "K" on page 74 of this record.

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

[File endorsement omitted.]

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[fol. 199] IN UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS, FIRST DIVISION

In Equity. No. 1646-N

CITIES SERVICE GAS COMPANY, Plaintiff,

against

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, J. W. Greenleaf, Thurman Hill, and Charles W. Camp-

bell, the Persons Constituting the Said Commission, and Roland Boynton, Attorney General of the State of Kansas; The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, The Pittsburg Gas Company, The Capital Gas & Electric Company, The Wyandotte County Gas Company, The Arkansas Valley Gas Company, The Girard Gas Company, and The Western Distributing Company, Defendants

BILL OF COMPLAINT—Filed Sept. 19, 1932

To said Honorable Court:

Comes now the plaintiff, Cities Service Gas Company, and files this, its bill in equity, and complaining of and against each and all of the above named defendants, respectfully avers:

[fol. 200] I

That the plaintiff is a private corporation duly organized and existing under the laws of the State of Delaware; that it is a citizen, resident and inhabitant of the State of Delaware, with its principal office located in the City of Dover, County of Kent, in said State. The plaintiff, having complied with all of the laws of the State of Kansas governing on the twelfth day of July, 1922, obtained from the Secretary of the State of Kansas a permit to do and transact business in the State of Kansas and that this plaintiff is now and has been ever since July 12, 1922, duly qualified to do business in the State of Kansas.

That the defendant The Wichita Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Wichita, County of Sedgwick, in the State of Kansas.

That the defendant The Hutchinson Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Hutchinson, County of Reno, in the State of Kansas.

That the defendant The Newton Gas Company is a corporation duly organized and existing under the laws of the

State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Newton, County of Harvey, in the State of Kansas.

That the defendant The Pittsburg Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant [fol. 201] of the State of Kansas, with its principal office located in the City of Pittsburg, County of Crawford, in the State of Kansas.

That the defendant The Capital Gas & Electric Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Topeka, County of Shawnee, in the State of Kansas.

That the defendant The Wyandotte County Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Kansas City, Counties of Wyandotte and Johnson, in the State of Kansas.

That the defendant The Arkansas Valley Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Arkansas City, County of Cowley, in the State of Kansas.

That the defendant The Girard Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Girard, County of Crawford, in the State of Kansas.

That the defendant The Western Distributing Company is a corporation duly organized and existing under the laws of the State of West Virginia; that it is a citizen, resident and inhabitant of the State of West Virginia, with its principal office located at Farmers Bank Building, at the corner of Wood Street and Fifth Avenue, in the City of Pittsburgh, County of Allegheny, in the State of Pennsylvania. [fol. 202] The defendant The Western Distributing Company having complied with all of the laws of the State of

Kansas governing, on the thirteenth day of September, 1906, obtained from the Secretary of State of Kansas a permit to do and transact business in the State of Kansas, so that this defendant is now and has been ever since September 13, 1906, duly qualified to do business in the State of Kansas.

The defendant J. W. Greenleaf is a citizen of the State of Kansas, and a resident and inhabitant of the County of Kiowa; that the defendant Thurman Hill is a citizen of the State of Kansas, and a resident and inhabitant of the County of Montgomery; that the defendant Charles W. Campbell is a citizen of the State of Kansas and resident and inhabitant of the County of Norton. That the defendant J. W. Greenleaf is chairman of The Public Service Commission of the State of Kansas, and that the defendants Thurman Hill and Charles W. Campbell are the sole remaining members of the said Commission, and that the last mentioned three defendants are the persons constituting the Public Service Commission of the State of Kansas, which is an administrative body duly created by the statutes of the State of Kansas, and will hereinafter be referred to collectively as the Public Service Commission; that the defendant Roland Boynton is the Attorney General of the State of Kansas, and is a citizen of the State of Kansas and a resident and inhabitant of the County of Lyon.

II

That this is a suit of a civil nature in equity and is brought under the authority of Section 266, as amended, of the Judicial Code of the United States for the purpose of restraining and enjoining, as far as affects this plain- [fol. 203] tiff, the enforcement of two certain orders of the said Public Service Commission dated August 31, 1932 (Exhibits "H" and "I" attached hereto), finding, among other things, that the defendant distributing companies are mere agents or instrumentalities of Cities Service Company, a Delaware corporation, that the contracts between the plaintiff and the defendant distributing companies under which the plaintiff sells gas to the defendant distributing companies respectively at the city gate at an average price of 39.5c per thousand cubic feet are unreasonable, and that the payments made thereunder are

excessive above the amount of 30c per thousand cubic feet for such main line town border gas, that 30c is a reasonable price to be paid the plaintiff by the defendant distributing companies respectively for main line town border gas and that any amount paid in excess thereof is unreasonable, and that on and after the first day of September, 1932, the defendant distributing companies shall cease to set up on their books as an expense item any payment made to the plaintiff for main line town border gas in excess of 30c per thousand cubic feet and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies, and, among other things, ordering that on and after the first day of September, 1932, the defendant distributing companies shall cease to set up on their books as an expense item any payments made to the plaintiff for main line town border gas in excess of 30c per thousand cubic feet and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies; and for the purpose of restraining and enjoining each of the defendant distributing companies from failing or refusing to carry out their respective agreements with the plaintiff for the purchase [fol. 204] of natural gas at the city or town border of the various communities served by the defendant distributing companies respectively at the rate, price or charge which each of the said defendant distributing companies has been and is now paying to the plaintiff for such gas, as more particularly stated hereinafter; and is a suit arising under the constitution and laws of the United States, in that, as plaintiff avers, the rate or price that said Public Service Commission directs each of the defendant distributing companies to pay to the plaintiff for natural gas is confiscatory of plaintiff's property used or useful in furnishing service and natural gas to the defendant distributing companies, and said order therefore seeks to deprive plaintiff of its property without due process of law, deny plaintiff the equal protection of the laws, to deny plaintiff freedom of contract and of business, all in violation of its rights under the Fourteenth Amendment to the Constitution of the United States, to impair the obligations of plaintiff's existing contracts in contravention of Article 1, Section 10 of the Constitution of the United States, to contravene Article

1, Section 8 of the Constitution of the United States commonly called the "Commerce Clause" of the said Constitution, all as hereinafter more fully set forth, and therefore said order of the Public Service Commission is null and void. The amount in controversy in this suit exceeds the sum or value of $3,000, exclusive of interest and costs.

III

For some years prior to January 1, 1928, plaintiff owned and operated a system of pipelines and appurtenances located in the States of Oklahoma, Kansas and Missouri, and was engaged in the production, transportation in inter- [fol. 205] state commerce, and the sale of natural gas as a continuous and established business. Additional supplies of gas being necessary for the conduct of business, plaintiff caused to be purchased in the State of Texas and elsewhere gas leases and rights, and caused to be constructed at great expense a pipeline connecting leases and sources of gas supply in the State of Texas and elsewhere to its said pipeline system above referred to, for the purpose of obtaining and transporting in interstate commerce for its present and future markets in Oklahoma, Kansas and Missouri gas owned and controlled by it in the State of Texas and elsewhere.

That from time to time and prior to the second day of July, 1931, plaintiff acquired and now holds and owns, along with other properties, the exclusive gas rights in and to approximately 1,225,000 acres of land situated in the States of Texas, Oklahoma, Kansas and elsewhere, and also as a part of its integrated, interstate pipeline system approximately 4,400 miles of pipelines in said states. That said gas acreage was acquired by the plaintiff in order to insure a dependable supply of natural gas for its customers and also to have dependable gas reserves to meet its future needs, and those of its customers and also to fulfill and carry out its contracts for the sale of gas.

That prior to the second day of July, 1931, plaintiff acquired and now owns, controls and operates an integrated, interstate natural gas pipeline and marketing system located in the States of Texas, Oklahoma, Kansas, Missouri and Nebraska. That plaintiff, by means of its above mentioned pipeline system, transports natural gas

in interstate commerce to various points in said states and delivers same in wholesale quantities to distributing companies, some of which are not affiliated with the plain- [fol. 206] tiff in any way, and also to the distributing companies, defendants in this action, under agreements and contracts lawfully entered into prior to the second day of July, 1931, and the plaintiff also, by means of its said pipeline system, delivers natural gas in wholesale quantities to other purchasers at wholesale under lawful contracts of sale providing for the delivery of such gas, which contracts were made and entered into prior to the second day of July, 1931, and all of which contracts are still in full force and effect.

IV

That plaintiff, prior to July 2, 1931, and relying upon its gas reserves acquired prior to that time for a constant and dependable source of supply, entered into numerous contracts whereby the plaintiff bound and obligated itself to furnish natural gas in wholesale quantities to many gas consumers and to numerous gas distributing companies in cities and towns in the States of Oklahoma, Kansas, Missouri and Nebraska.

That among the contracts so entered into by the plaintiff were contracts with The Wichita Gas Company to supply it with natural gas at the city border of Wichita, Kansas, for distribution to the industries and inhabitants of the said City, with The Hutchinson Gas Company to supply it with natural gas at the city border of Hutchinson, Kansas, for distribution to the industries and inhabitants of the said City, with The Newton Gas Company to supply it with natural gas at the city border of Newton, Kansas, for distribution to the industries and inhabitants of the said City, with The Pittsburg Gas Company to supply it with natural gas at the city border of Pittsburg, Kansas, for distribution to the industries and inhabitants of the said City, with [fol. 207] The Capital Gas & Electric Company to supply it with natural gas at the city border of Topeka, Kansas, for distribution to the industries and inhabitants of the said City, with The Wyandotte County Gas Company to supply it with natural gas at the city border of Kansas City, Kansas, for distribution to the industries and inhabitants of the said City, with The Arkansas Valley Gas Com-

pany to supply it with natural gas at the city border of Arkansas City, Kansas, for distribution to the industries and inhabitants of the said City; with The Girard Gas Company to supply it with natural gas at the city border of Girard, Kansas, for distribution to the industries and inhabitants of the said City, and with The Western Distributing Company to supply it with natural gas at the city borders of twenty-seven towns in the State of Kansas for distribution to the industries and inhabitants of the said cities. That all of the above named companies are defendants in this action (all of such defendants herein being referred to for brevity as the "defendant distributing companies") and distributing companies supplying gas which is furnished to each of them by the plaintiff, which they in turn supply and deliver at retail to domestic consumers in each of said respective cities and towns for heating, lighting and other purposes, and to various manufacturers and industrial plants. That in the nature of things, any interruption, cessation or failure of supply of natural gas will be disastrous to the comfort and health of such domestic consumers and deleterious to the business of those industrial and manufacturing concerns which utilize gas in their operations.

That the plaintiff, for a long time prior to July 2, 1931, and since that time, has been and now is supplying natural gas to each of the defendant distributing companies at the town border of each of the cities and towns served re- [fol. 208] spectively by the defendant distributing companies at a reasonable rate and price under agreements with each of said defendant distributing companies. That the rates or prices at which the plaintiff has been and is now supplying the defendant distributing companies with natural gas as aforesaid are: to The Wichita Gas Company at 40c per thousand cubic feet; to The Hutchinson Gas Company at 40c per thousand cubic feet; to The Newton Gas Company at 40c per thousand cubic feet; to The Pittsburg Gas Company at 38c per thousand cubic feet; to The Capital Gas & Electric Company at 40c per thousand cubic feet; to The Wyandotte County Gas Company at 40c per thousand cubic feet; to The Arkansas Valley Gas Company at 15c per thousand cubic feet; to The Girard Gas Company at 38c per thousand cubic feet; and to The Western Distributing Company at 40c per thousand cubic feet. That

all of the agreements under which the plaintiff has been and now is supplying gas to each of the defendant distributing companies are reasonable and lawful and were entered into by the plaintiff and each of the defendant distributing companies after negotiations looking to the protection of the plaintiff as well as to each of the defendant distributing companies, and after each of the parties thereto had taken into consideration and reflected upon the gas reserves of the plaintiff, the dependability of its source of gas supply and the pipelines and facilities of the plaintiff for properly furnishing the same without interruption.

V

That on or about the second day of July, 1931, the defendants, the said The Public Service Commission of Kansas, J. W. Greenleaf, Thurman Hill and Charles W. Campbell, composing the Public Service Commission of the State of Kansas, all of said defendants being herein referred to as the Public Service Commission, ordered that the reasonableness of all contracts and charges made by holding companies to the defendant distributing companies above named, operating in the State of Kansas, should be inquired into for the purpose of determining the reasonableness of such contracts and the reasonableness of charges made for services and commodities furnished to each of the defendant distributing companies and for that purpose the said Public Service Commission ordered that an investigation be set for hearing on the 18th day of August, 1931, at Topeka, Kansas, to inquire into the reasonableness of contracts made with and services rendered to the defendant distributing companies and other distributing companies, and further ordered that each of the defendant distributing companies appear on the above mentioned date to give to the Public Service Commission such information as they may desire on their own behalf and as may be required by the Commission on behalf of the said investigation and to show cause, among other things, why service or commodity charges made to the defendant distributing companies, including a charge of this plaintiff for the furnishing of natural gas to each of the defendant distributing companies, should such charges be found to be unreasonable, should not be disallowed as operating expenses of the

[fol. 209]

defendant distributing companies, and adjustment made in this respect as to the charges made to the consumers by the defendant distributing companies.

That on the 17th day of August, 1931, said Public Service Commission ordered that such investigation be continued and set for hearing on the 19th day of October, 1931, at the same place.

[fol. 210] That on October 16, 1931, each of the defendant distributing companies filed a special appearance before the said Public Service Commission. Counsel for the defendant distributing companies, in making such a special appearance for each one thereof, made statements, copies of which are attached to this bill of complaint and marked Exhibit "A," which statements set forth the views of counsel for each of the defendant distributing companies as to the nature and extent of the investigation by said Public Service Commission and the special appearance entered on the record.

In these statements, among other things, counsel for the defendant distributing companies stated that each of the defendant distributing companies joined in one order and involved in one hearing are separate and distinct properties serving some 128 cities and communities; that the rates of each system must of necessity be based on the value of its property and its financial experience; that the statutes of Kansas contemplate separate hearings and provide for review of the courts on the record of that property, the venue being determined by the location of the property; that the defendant distributing companies enter said proceeding with the definite contention that it is not a rate case as to any particular property and involves no consideration of the reasonableness or unreasonableness of the rates charged by the defendant distributing companies to their respective consumers; that the most important matter the said Public Service Commission claims a right to investigate is the rate paid for gas by the several distributing companies defendants herein at the city gate, but that the distributing companies would lay all the facts before the said Commission in the said proceeding; that the existing rate charged by the plaintiff for natural gas to be delivered at [fol. 211] the city gate of each of the defendant distributing companies has twice been held reasonable by the courts,

including the highest court of the State of Kansas. Counsel for the defendant distributing companies further stated that the order of the said Public Service Commission dated the second day of July, 1931, seems to contemplate that should the said Commission find forty cents to be too high at the city gate it should be reduced to, say, thirty-five cents or thirty cents; that the reduction of five or ten cents should be adjusted immediately as to each company without a separate hearing as to the needs and requirements of that particular company.

That the hearings in said investigation before said Commission were held from time to time and evidence and exhibits were introduced by the respondent distributing companies in said investigation to show that the contracts between the plaintiff and the defendant distributing companies, the respondents in said investigation before the Public Service Commission, under which the plaintiff sells natural gas to the defendant distributing companies at the city gates for forty cents per thousand cubic feet and in some cases less, were reasonable and such contracts as would be made by perons dealing at arm's length; that the rate or price which the plaintiff charges to the defendant distributing companies at the city gate is fair and reasonable; that the fair value of the property of plaintiff on September 1, 1931, used or useful in its business of supplying natural gas to the defendant distributing companies was $105,857,402 and that its net earnings from operation after depreciation available for the return on said value for the year ending June 30, 1931, was $5,455,032.25, or 5.16% on said return base of $105,857,402, which rate was and is inadequate, unreasonable and confiscatory of plaintiff's property.

[fol. 212] That in the course of the said investigation before the said Public Service Commission each of the defendant distributing companies were prohibited by the said Public Service Commission from introducing any evidence to show the value of the property of each of the said defendant distributing companies used or useful by each thereof in its business of distributing natural gas to the inhabitants of the community which it served and were also prohibited from showing their respective earnings, expenses and their net earnings and the percentage of return which each of the said distributing companies was receiving, based upon

its net earnings and the value of its property used or useful in its business, although each of the said defendant distributing companies asked permission to do so and offered to introduce such evidence for the purpose of showing the rate of return which each of the said defendant distributing companies was making was inadequate, unreasonable and confiscatory.

## VI

That on the 20th day of July, 1932, the said Public Service Commission of the State of Kansas handed down its opinion and order dated the 20th day of July, 1932.

That in this order the Commission found that the contracts between the plaintiff and the defendant distributing companies respectively under which the plaintiff sells gas to said defendant distributing companies at the city gates at an average price of 39.5 cents per thousand cubic feet are unreasonable, and that the payments made thereunder are excessive in the amount of 10 cents per thousand cubic feet for such main line town border gas; that 29.5 cents is a reasonable price to be paid the plaintiff by each of the [fol. 213] defendant distributing companies for main line town border gas and that any amount paid in excess thereof is unreasonable and are not such contracts as parties dealing at arm's length would enter into; that on and after the 1st day of August, 1932, defendant distributing companies shall cease to set up on their books as an expense item any payments paid to the plaintiff for main line town border gas in excess of 29.5 cents per thousand cubic feet, and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies.

## VII

That thereafter, and on or about July 30, 1932, each of the defendant distributing companies filed with the said Public Service Commission of the State of Kansas an application for a rehearing, a copy of which (which is the one filed by the defendant distributing company The Arkansas Valley Gas Company) is attached to this bill of complaint and marked Exhibit "B." Each of the defendant distrib-

uting companies filed with the said Commission a similar application for rehearing, properly signed and verified. That in said applications for rehearing each of the defendant distributing companies, fully reserving all their rights as set out in the special appearance contained in Exhibit "A," applied for rehearing in respect to all matters found and ordered by the said Public Service Commission of the State of Kansas, and purported to have been determined by the said Commission for the reason that its decision, findings and order severally and collectively were unlawful, unjust and unreasonable in the respects set forth in said Exhibit "B."

[fol. 214] VIII

That on the first day of August, 1932, the Commission, having before it for consideration the said application for a rehearing, ordered that defendant distributing companies and respondents in said investigation before said Public Service Commission submit to the Commission on or before August 4, 1932, a complete earning and expense statement for the plaintiff covering the year ending June 30, 1932, a copy of which order for information is hereto attached and marked Exhibit "C." That it was recited in the said order that the Commission desired said information in order to enable it to give proper consideration to the application for a rehearing, Exhibit "B," and also in said order said Commission found that information should be included showing to the Commission loss in revenue due to reductions in the price of gas sold by the plaintiff, the amount paid to Henry L. Doherty & Company for the year ending June 30, 1932, and what adjustment was made for construction credit, if any.

That each of the defendant distributing companies and respondents in said investigation before said Public Service Commission on August 4, 1932, filed with the Commission an answer to the said order for information of August 1, 1932, Exhibit "C" similar to the answer filed by the defendant distributing company The Pittsburg Gas Company, copy of which is hereto attached and marked Exhibit "D." That each of the defendant distributing companies in said answer, without recognizing the jurisdiction of the said Commission to issue the said order of August 1, 1932, Ex-

hibit "C," and without waiving their rights to contest the validity thereof, alleged, among other grounds, that under [fol. 215] the statutes of the State of Kansas the proceedings before said Commission were closed by the issuance of its order of July 20, 1932, and that the Commission was without jurisdiction or authority to reopen the same for consideration of further evidence other than by granting respondents' application for rehearing.

That on the fifth day of August, 1932, the said Public Service Commission granted the application of each of the defendant distributing companies respondents in the said investigation before the Public Service Commission and directed that a rehearing be held on the 15th day of August, 1932, at the State House, Topeka, Kansas, at which time the said defendant distributing companies, respondents in the said investigation, would be given an opportunity to present evidence in behalf of their allegations as to the earnings of the plaintiff for the year ending June 30, 1932, and the said Public Service Commission further ordered that its order issued on July 20, 1932, be suspended pending final disposition of the matter after hearing, a copy of which order granting a rehearing is attached to this bill of complaint and marked Exhibit "E."

That thereafter, and on the fifteenth day of August, 1932, a rehearing was held by the said Commission at Topeka, Kansas, at which time each of the defendant distributing companies introduced in evidence an earning statement showing the earnings of the plaintiff for the year ending June 30, 1932.

That at said rehearing each of the defendant distributing companies offered to prove, among other things, that in entering into the contract with the plaintiff for a supply of natural gas to be delivered from plaintiff's main line at the town border of the various communities served by the defendant distributing companies, respectively, each of the [fol. 216] defendant distributing companies were advised of and relied upon the gas reserves of the plaintiff for a constant, dependable supply of gas and offered to show that all of the gas acreage and reserves of the plaintiff were necessary to assure to each of the said defendant distributing companies an adequate and constant supply of natural gas for their needs, and that the pipeline companies obtaining natural gas from the Amarillo field in Texas

were only taking approximately 17% of the gas allowed to be taken from the said field, and the balance of the gas taken from said field is used for gasoline and carbon black plants and the production of oils, or wasted, and the Railroad Commission of the State of Texas has under consideration ordering that all takes of gas from wells be limited to 5% of the open flow of such wells and that all wells having unconnected offset wells be shut down, and that the threatened and contemplated action of the Railroad Commission of the State of Texas, if put into effect this coming winter, would prevent plaintiff from supplying each of the defendant distributing companies with an adequate and dependable supply of natural gas from the Amarillo field, and the plaintiff would necessarily have to draw on its gas reserves in other fields.

That attached to this bill of complaint and marked Exhibit "F" is a copy of said offer of proof presented to the said Public Service Commission at said rehearing by each of the defendant distributing companies herein.

That the said Public Service Commission wrongfully and unlawfully denied to each of the defendant distributing companies the right to make such proof and refused to listen to or permit each of the defendant distributing companies to make any proof whatsoever of the facts offered to be proved before the said Commission by each of the [fol. 117] defendant distributing companies as set forth in Exhibit "F."

That the said Commission only permitted proof of the earnings and expenses and net income of the plaintiff for the year ending June 30, 1932.

## IX

That on the 31st day of August, 1932, the said Commission rendered an opinion, a copy of which is attached to this bill of complaint and marked Exhibit "G"; that based upon the said opinion the said Commission issued two orders dated August 31, 1932, copy of which orders are attached to this bill of complaint and marked Exhibits "H" and "I."

That on the 9th day of September, 1932, each of the defendant distributing companies filed with the Public Service Commission of Kansas a second application for re-

hearing, copy of which is annexed to this bill of complaint and marked Exhibit "J."

That thereafter on September 10, 1932, said defendant distributing companies each filed a supplemental application for rehearing, a copy of which is hereto attached marked Exhibit "K" and made a part hereof.

That on the 12th day of September, 1932, the said Public Service Commission entered an order denying said applications for rehearing.

X

That at no time has the plaintiff held itself out as a public utility or common carrier of gas, nor has it at any time engaged in the business of a common carrier. That the entire properties, gas reserves, pipelines and appurte- [fol. 218] nances of the plaintiff have been from the inception of their acquisition by plaintiff and now are devoted exclusively to the plaintiff's private enterprise and business of producing gas from its own properties, transporting the same through its own private pipelines in the states of Texas, Oklahoma, Kansas, Missouri and Nebraska. That plaintiff's gas from the time it begins to move from its position in place within plaintiff's gas lands until the time it is delivered to the defendant distributing companies and others, moves in a continuous and unbroken flow through plaintiff's private pipelines and in interstate commerce. That plaintiff was not and could not have been made a party to said proceeding or investigation before the Public Service Commission of the State of Kansas, did not submit itself to the jurisdiction of the said Commission and therefore has not been afforded or given an opportunity to be heard with respect to the matters and things set forth in this bill of complaint. That the plaintiff's existing contract charges for gas transported in interstate commerce and sold and delivered to each of the defendant distributing companies at the town border of the various communities served by the said defendant distributing companies were in existence prior to the said investigation by said Public Service Commission and were in existence at the date of the said order, Exhibit "H," and that such charges and rates are fair and reasonable.

XI

That the fair and reasonable value of the plaintiff's property used or useful in its business as it existed on the 30th day of June, 1932, is the sum of $105,857,402.00.

That the least fair annual return which the plaintiff is [fol. 219] entitled to earn is an amount equal to not less than eight per cent (8%) of the fair and reasonable value of its property used or useful in the rendition of the services it performs, over and above a proper allowance for replacement reserves. That such a proper annual allowance for replacement reserves should be $3,276,325.07.

That plaintiff's net earnings from operation derived from its said interstate pipeline and gas transportation business for the year ending June 30, 1932, were $7,861,516.85. That after deducting proper annual depreciation allowances of $3,276,325.07 there remains a return upon the fair and reasonable value of the plaintiff's property used or useful in furnishing gas service and exclusively devoted to the rendition thereof for the year ending June 30th, 1932, of four and three tenths (4.3%) per cent.

That the said Public Service Commission in the said investigation found that the value of the plaintiff's property used or useful in its business was only $73,148,510.00 and found that the plaintiff's annual depreciation allowance should be $1,977,591.00. On the said rate base found by the Public Service Commission after deducting therefrom the allowance above set forth, as found by the Commission, the plaintiff would only receive an annual return of 8.04% on the value of its property as erroneously determined by the said Commission. This clearly demonstrates that the contracts which the plaintiff is and has been operating under in selling gas to the defendant distributing companies are not unreasonable but are fair and reasonable, and the rates, charges or prices which the plaintiff makes to the defendant distributing companies for supplying them with natural gas are not excessive or unreasonable, and [fol. 220] that the contracts are such as would have been entered into by persons dealing at arm's length with respect to the same subject-matter.

That the plaintiff's business has been conducted efficiently and economically during all the times herein referred to.

That said opinion and the findings therein contained and the said orders and the findings therein contained, respec-

tively (Exhibits "G," "H" and "I" attached hereto), are unlawful, unjust, unreasonable, confiscatory, void and unconstitutional as respects this plaintiff for, among others, the following reasons:

(a) For the reason that the Public Service Commission, in its investigation of the contracts between plaintiff and the defendant distributing companies for the supply of gas at the city or town borders of the respective communities served by the defendant distributing companies, approached all questions involving the same as if it had power and jurisdiction under the law to fix the rates and commodity charges of the plaintiff and has in effect undertaken to fix the rates and commodity charges of the plaintiff in relation to its interstate business, and the Public Service Commission has undertaken to and has fixed the rates and commodity charges for the plaintiff, and by its decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) said Public Service Commission has usurped a power to regulate and burden interstate commerce and has acted wholly without constitutional or lawful authority, power or jurisdiction;

(b) For the reason that the gas purchased by the defendant distributing companies, respectively, at the respective town borders of the various communities served by them is natural gas transported by plaintiff in interstate commerce, national in its character, and plaintiff is lawfully [fol. 221] entitled to sell said gas to the several defendant distributing companies herein and to other purchasers in the several states through which plaintiff's transportation system passes without interference by the said Public Service Commission of the State of Kansas or any other state in which said interstate transaction is carried on, and said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) unlawfully deprive the plaintiff of the benefits and advantages of its ownership of said gas and said pipeline system and the fruits of its said interstate transportation, and unlawfully deny to the plaintiff the free right to sell from its said transportation system its natural gas so transported, and unlawfully deprives the plaintiff of the rights guaranteed to the plaintiff by Article 1, Section 8, Clause 3, of the Constitution of the United States;

(c) For the reason that the decision, opinion, findings and orders of the Public Service Commission (Exhibits "G," "H" and "I" attached hereto) and each and every part of both thereof, are in violation of Article 1, Section 8, Clause 3, of the Constitution of the United States in that said decision, opinion, findings and orders seek to impose upon the plaintiff an unreasonable regulation and place an undue burden on interstate commerce;

(d) For the reason that the decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) are in violation of Article 1, Section 10, first subdivision of the Constitution of the United States in that they and each of them impair the obligation of the contracts of the plaintiff with each of the several defendant distributing companies under which each of said defendant distributing companies purchase gas from the plaintiff;

(e) For the reason that said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) [fol. 222] are in violation of the Fourteenth Amendment to the Constitution of the United States in that they deprive the plaintiff of its property without due process of law, destroy its freedom of contract and deny to it the equal protection of the laws;

(f) For the reason that the order of the Commission (Exhibit "H" attached hereto) directing that each of the defendant distributing companies shall cease to set up on their books as an expense item any payments made to plaintiff for main line town border gas in excess of 30 cents per thousand cubic feet and shall give no consideration to any such payments in fixing a rate for their domestic consumers, and the findings of the said Commission in the said order that the contracts between the plaintiff and the defendant distributing companies, under which the plaintiff sells gas to the said defendant distributing companies at the city gate at an average of 39.5 cents per thousand cubic feet, are unreasonable and that the payments made under such contracts are excessive above the amount of 30 cents per thousand cubic feet for such main line town border gas supplied to the defendant distributing companies by the plaintiff, fixes a rate, charge or price that would not produce a reasonable return on the fair value of the property

of the plaintiff used or useful in furnishing its interstate gas service to the defendant distributing companies and others, and that if the plaintiff were required to deliver gas to the distributing companies at a rate of 30 cents per thousand cubic feet, it would result in the confiscation of the plaintiff's property and deprive the plaintiff of its property without due process of law, all in violation of the Fourteenth Amendment to the Constitution of the United States;

[fol. 223] (g) For the reason that the plaintiff, in the sale of its said products so transported in interstate commerce, is limited to the market connected with its transportation system, as now located, and that if the said orders of the Public Service Commission (Exhibits "H" and "I" attached hereto) are enforced it will in effect deprive the plaintiff of all market for its gas at rates and charges other than those attempted to be established by the said Public Service Commission in its said decision and orders (Exhibits "G," "H" and "I" attached hereto) and deprive the plaintiff of the right to carry on its business and deprive it of its property without due process of law, all in violation of the Fourteenth Amendment to the Constitution of the United States;

(h) For the reason that said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) in so far as they relate to the contracts between the plaintiff and the defendant distributing companies, and under which said defendant distributing companies respectively purchase the supply of gas for distribution to their consumers, impair the operation of such contracts; deny to plaintiff the free right of contract, undertake the business management of the plaintiff; usurp the duties of the officers and directors of the plaintiff and substitute the opinion, judgment and conclusions of the said Public Service Commission for the business opinion and judgment of the officers and directors of the plaintiff as to matters of purely business policy, all in violation of the Constitution of the United States and its amendments;

(i) For the reason that plaintiff has informed and notified each of the defendant distributing companies that plaintiff will not supply said distributing companies with gas at the

rate and charge directed by the Commission in said opinion and order, to-wit: 30 cents per thousand cubic feet at the [fol. 224] city gates of the various communities served by the defendant distributing companies, and if the plaintiff has no other remedy than to do this, such action on its part will undoubtedly result in a multiplicity of suits and in irreparable damage;

(j) For the reason that in the said investigation the said Commission refused to permit the defendant distributing companies to prove that the gas reserves of the plaintiff are all necessary in order to guaranty the fulfillment of the plaintiff's contracts with the defendant distributing companies and to plaintiff's other customers on said system; that the gas reserves of the plaintiff of 71,267 acres allowed by the Commission are inadequate; that said 71,267 acres allowed by the Commission do not contain the gas reserves available to the plaintiff which the Commission found they would have; that during 1931 the total volume of gas taken from the Texas Panhandle gas field was 1,263,000,000 cubic feet per day, of which only 219,000,000 cubic feet per day were taken by the pipelines running into the said field, including that of the plaintiff, or that the pipelines, including that of the plaintiff, only took 17% of the total gas taken from the said Panhandle field; that the gas not taken by pipelines from said field was used by others than the plaintiff in gasoline plants, carbon black plants, production of oils, or blown into the air, and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Railroad Commission of the State of Texas; that said Railroad Commission of the State of Texas has under consideration an order limiting all gas taken from the wells to 5% of the open flow from such wells, and an order shutting in all gas wells having offset wells unconnected with any pipeline; that if the Railroad Commission of the State of Texas makes the proposed order [fol. 225] and it is enforced, the 71,267 acres allowed by the said Public Service Commission of the State of Kansas will be wholly inadequate to supply gas for the needs and requirements of the plaintiff for even the coming winter, and if plaintiff restricts its takes of gas from the said field to the average allowed by the Railroad Commission of the State of Texas its service to the communities in Kansas will

fail; that under present practices in the State of Texas the owners of approximately 10% of the gas leases are producing approximately 82% of the gas produced from the said field, none of which is connected to pipelines, including that of plaintiff, or used by such pipelines; that such practices have reduced the rock pressure in the Borger territory in the State of Texas from the original rock pressure of 430 pounds per square inch to less than 50 pounds per square inch; that gas in the area including the 71,267 acres allowed by the Public Service Commission of the State of Kansas is migrating to the low pressure Borger area; that the reserves of gas under the said 71,267 acres are being thus constantly depleted and are not available to the plaintiff as assumed by the said Public Service Commission of the State of Kansas; that in the computation of the said Public Service Commission of the State of Kansas of proper gas reserves for this plaintiff, said Commission included the open flow of wells sold to the Texoma Natural Gas Company, amounting approximately to 250,000,000 cubic feet per day, which is not available to the plaintiff; that all of these matters should have been taken into consideration in determining the proper gas reserves which the plaintiff is entitled to and which its officers and directors deem proper, and that such matters were not taken into consideration by the said Public Service Commission of the State of Kansas; [fol. 226] that the gas reserves of the plaintiff in all states are not in excess of proper gas reserves as recognized by the gas business and industry and as compared to the gas reserves held by other major pipeline companies, and that none of the gas acreage or reserves now held by the plaintiff was bought or is being held by the plaintiff for speculation or other purpose other than to supply its customers with an adequate supply of natural gas and to fulfill its existing contracts; and that the said Public Service Commission refused to take into consideration the fair market value of all of the plaintiff's gas acreage in determining the value of plaintiff's property used or useful in its business;

(k) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) are void in that they undertake to put into effect reduced rates and charges for the gas delivered to the defendant distributing

companies by the plaintiff as of September 1, 1932, and that said order is contrary to the statutes of the State of Kansas;

(l) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) direct an unreasonable, unjust and unlawful discrimination in that said orders direct that gas sold by the plaintiff to the respective defendant distributing companies be sold at a rate different from that plaintiff sells gas to other distributing companies not affiliated with plaintiff;

(m) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) are the result of the erroneous action of the said the Public Service Commission of the State of Kansas in attempting to average the fair value of the plaintiff's property and earnings over certain periods of time and by its failure to include the value of certain items of property and of certain gas acre-
[fol. 227] age used or useful in the plaintiff's business, and computed plaintiff's earnings on the value of the property allowed by the Commission on a much lower rate base than actually existed, and on which such earnings should have been computed, and that such valuation of plaintiff's property made by the said the Public Service Commission of the State of Kansas is not the fair value of the property of the plaintiff on September 1st, 1931, or on June 30, 1932, and that the earnings of the plaintiff on the erroneous rate base found by the said Commission are not the earnings of the plaintiff as of the thirtieth day of June, 1932, which earnings on the fair value of the plaintiff's property on June 30, 1932, were not in excess of a fair and reasonable return on the fair and reasonable value of its property used or useful in its business, and therefore its contracts with the defendant distributing companies were and are fair and reasonable and such as would have been made by parties dealing at arm's length;

(n) For the reason that the said Public Service Commission unlawfully and unreasonably usurped the prerogatives, duties and authorities of the officers and directors of the plaintiff, upon whom the responsibility for managing the plaintiff and for the plaintiff's service rests, and arbitrarily and unlawfully refused to include in the rate base

of the plaintiff and in the value of its property, leases of the fair market value of many millions of dollars, for the alleged reason that said leases were not, in the opinion of the Commission, presently used or useful and thus the effect will be to deprive the plaintiff of its property without due process of law, contrary to the Constitution of the United States;

(o) For the reason that the said the Public Service Commission of the State of Kansas, in its investigation resulting in the said orders (Exhibits "H" and "I" attached [fol. 228] hereto), eliminated from the operating expenses of plaintiff rentals and charges on gas leases, which leases, in the business judgment of the officers and directors of the plaintiff, are necessary to hold and maintain in order to constitute and insure an adequate, proper and necessary gas reserve for plaintiff's pipeline system to fulfill its contracts and supply its customers with natural gas, and eliminated certain other proper items of expense, thereby unreasonably and unlawfully substituting the said Public Service Commission's opinion for the business judgment of the officers and directors of the plaintiff, in violation of the Fourteenth Amendment to the Constitution of the United States;

(p) For the reason that the said Commission, in its investigation resulting in the said orders (Exhibits "H" and "I" attached hereto), in finding the value of the property of the plaintiff and in allowing replacement reserves, arbitrarily disregarded and ignored testimony and evidence introduced before the said Public Service Commission and uncontradicted with respect to such value and replacement reserves, and thus indirectly deprived the plaintiff of its property without due process of law, in violation of the Constitution of the United States.

(q) For the reason that the said Public Service Commission, in its investigation resulting in said orders (Exhibits "H" and "I" attached hereto), illegally and unlawfully refused to consider or allow certain intangible items of value which should have been allowed in determining the fair value of the property of the plaintiff, upon which the plaintiff was and is entitled to earn a fair and reasonable return;

(r) For the reason that the said Public Service Commission of the State of Kansas has no power or jurisdiction over this plaintiff but that notwithstanding, and in a pro-[fol. 229] ceeding to which this plaintiff was not and could not have been made a party, the said the Public Service Commission of the State of Kansas has made the said orders wherein and whereby this plaintiff is deprived of its rights and properties, and the benefits, advantages and obligations of its contracts without due process of law and in violation of plaintiff's rights under the Constitution of the United States.

XII

That if plaintiff is forced and compelled by reason of the orders of the said Commission (Exhibits "H" and "I" hereto attached) to supply gas to the defendant distributing companies for 30 cents per thousand cubic feet, the compensation it will receive for the said gas will not afford the plaintiff a fair return upon the fair and reasonable value at the time of the use of its property, used or useful in and exclusively devoted to such service, but its return will be confiscatory in effect.

That if the said orders of the Public Service Commission (Exhibits "H" and "I" hereto attached) are enforced against one or more of the defendant distributing companies, such enforcement coercing and compelling each of the defendant distributing companies to violate their respective contracts with the plaintiff for the purchase of gas at the rates now in force by virtue of such contracts, the result will be that by reason of such illegal, unreasonable, unlawful and confiscatory orders and in consequence thereof plaintiff's business and property will be destroyed and the freedom of its interstate business materially interfered with and burdened and its freedom of contract destroyed.

[fol. 230] That the said orders of the said Public Service Commission (Exhibits "H" and "I" hereto attached) are void and in excess of the authority conferred by law upon the said Public Service Commission and further in that said orders deprives the plaintiff of an opportunity to have a judicial determination as to the legality of its contracts and charges to each of the defendant distributing companies by arbitrarily requiring the plaintiff to

reduce its charges for its gas to each of the defendant distributing companies as of September 1, 1932, whether said charges be finally sustained as legal or not; and the said order further on this account seeks to deprive the plaintiff of its property and business without due process of law and deny the plaintiff equal protection of the laws under the Fourteenth Amendment to the Constitution of the United States, and to impair the obligations of its contracts with each of the defendant distributing companies contrary to Section 10 of Article 1 of the Constitution of the United States, and for these reasons said order is null and void.

XIII

That unless the defendants the Public Service Commission of the State of Kansas and members comprising it, are restrained and enjoined as herein prayed, they will, as plaintiff believes and so alleges, attempt to compel the plaintiff and each of the defendant distributing companies, and thus the plaintiff, to comply with the said orders of the Public Service Commission (Exhibits "H" and "I" attached hereto) and to enforce the penalties prescribed by the laws of the State of Kansas for failure to comply with said orders (Exhibits "H" and "I") and the defendant [fol. 231] distributing companies, their respective officers, agents and employees, will be deterred and prevented by the threat of said penalties from carrying out their contracts with plaintiff and from paying to plaintiff the rates and charges which each of the defendant distributing companies have been and are now paying to the plaintiff for natural gas at the town border of the various communities served respectively by the defendant distributing companies and thereby plaintiff will be forced to submit to the confiscation of its property without due process of law and in violation of its rights under the Constitution of the United States as herein alleged, and will be subject to great and irreparable loss and damage.

That plaintiff has heretofore and prior to the thirty-first day of August, 1932, notified the defendant distributing companies that it will not supply them with natural gas except on the basis of the charges and rates in force between the plaintiff and the defendant distributing com-

panies now and prior to the second day of July, 1931, by virtue of the agreements between the plaintiff and the said respective distributing companies; and that for the plaintiff to sell and deliver gas to the defendant distributing companies at the prices fixed by the Public Service Commission in its orders (Exhibits "H" and "I" attached hereto) would not afford the plaintiff a fair and reasonable return on the value of its property used or useful in its business, and would result in the confiscation of its property and business.

XIV

That as further ground for its cause of action plaintiff says that during all the times involved herein, the majority of the voting capital stock of plaintiff has been owned by Empire Gas and Fuel Company, a Delaware corporation. [fol. 232] That of the capital stock of said Empire Gas and Fuel Company a large majority in nominal or par value of said stock is owned by individuals entirely disconnected with Cities Service Gas Company and with Cities Service Company hereinafter mentioned who are citizens of many different states of the Union. These persons own preferred stock of said Empire Gas and Fuel Company to the amount of approximately fifty-four million dollars ($54,000,000.00) in par or nominal value and are entitled to the receipt of profits through dividends before any dividends upon common stock of said Empire Gas and Fuel Company are declared or paid. That Cities Service Company owns a majority of the common stock of said Empire Gas and Fuel Company, and also owns a majority of common stock of Gas Service Company, which latter corporation owns a majority of the common stock of all the distributing companies made defendants herein. That while within the technical provisions of Chapter 239 of the Session Laws of the State of Kansas for 1931, plaintiff is affiliated with each of said distributing company defendants, yet its officers and actual managing agents are for the most part entirely different and the employees of the plaintiff have very little contact with, knowledge of, or acquaintance with the employees of each of said distributing company defendants, and their businesses are for all practical purposes carried on in as independent a manner as if such affiliation did not exist, and the great bulk of the ownership of the Empire

Gas and Fuel Company stock in persons entirely disconnected with any other companies prevents the plaintiff or said distributing companies from being made mere instruments of the other, or the mere instrument of Cities Service Company. That the great majority of stockholders of said [fol. 233] Empire Gas and Fuel Company would receive no benefit whatever from enhanced profits of said distributing company defendants, and the stockholders of said distributing company defendants could not in any wise be benefited by or participate from profits of the plaintiff Cities Service Gas Company. That the said distributing companies, defendants, and this plaintiff have occupied such status with relation to each other during all times involved herein.

XV

That for more than twenty-five years just last passed the plaintiff and its predecessors and grantors have been engaged in the business of transporting natural gas into Kansas from Oklahoma or Texas, or both, as the case may be; that said business passed into the hands of this plaintiff in 1922 and ever since has been and now is owned and operated by plaintiff. That said business during all the time involved herein has been and is now transacted by means of an integrated interstate pipeline system lying in the states of Texas, Oklahoma, Kansas, Missouri and Nebraska, and the same is one integral enterprise and the plaintiff has no other business than that transacted by said integrated system of pipe lines. That in said business, plaintiff has a capital investment of approximately one hundred million dollars. That in the well established course of its said business plaintiff customarily contracts with distributors or other wholesale consumers for the delivery of the gas carried through its said pipeline system before the said gas starts from its place of production in other states, and in order that its said system should effectually and adequately serve the needs of its customers in the State of Kansas, plaintiff has built pipe lines of large capacity and [fol. 234] at proper intervals along the said lines has installed powerful and expensive compressor stations, each composed of many separate power units that may be thrown into or taken out of operation upon a moment's notice to meet the fluctuating demands of its markets, both hourly or

seasonally, and because of the necessity of supporting enormous peaks in times of very cold weather in order that the consumers of its customers might not suffer with cold, it has, because of the consideration that natural gas is a wasting asset, that a given gas field may be unexpectedly and suddenly destroyed by the intrusion of water or other unforeseen disturbances, that the several states have restrictive laws and rules upon the portion of the open flow of a well that may be taken and because of a likelihood of unexpected and radical regulations being at any time imposed by the authorities having jurisdiction of gas conservation in the several states where plaintiff's gas reserves are to control the production from any given field, and other uncertain and hazardous contingencies this plaintiff has been compelled to and in the exercise of its best business judgment has acquired gas leasehold estates of an acreage of approximately 1,225,000 acres in the various states from which it draws its supplies of gas. That plaintiff and its predecessors in said business have already exhausted in the proper conduct of said business which has been a constantly increasing business gas lands of an aggregate area far in excess of the gas reserves it now owns and by reason of such experience plaintiff well knows the necessity of having at all times an adequate reserve and how much reserve is reasonably necessary. That said defendant The Public Service Commission without any knowledge on this subject and without any effort to learn or be informed as to the past experience of plaintiff and its predecessors, [fol. 235] arbitrarily and capriciously substituted its judgment for the judgment of the officers and directors of plaintiff and found that 71,267 acres of gas leases located in Texas, Kansas, Missouri and Oklahoma, was ample and sufficient for plaintiff to adequately supply its customers for a period of twenty-two years, and wrongfully excluded from its valuation of plaintiff's property all other gas leases owned by it. That all of said gas reserve was acquired for the single enterprise composing plaintiff's business and is reasonably necessary to the continuous and dependable operation of the same, and that no person however skilled in the gas industry is able to say for any considerable period in advance at what particular time this plaintiff will be compelled to resort to any given portion of

its said gas reserve for supplying the demands of its customers and meeting the seasonal exigencies of its business.

XVI

That the defendant distributing companies are each and all public service corporations purchasing gas from plaintiff at wholesale at their respective city gates under contract to pay a specified amount, which gas they in turn sell to the inhabitants of the respective cities they serve and their environs. That ever since the year 1911, in which the first public utility law of the state of Kansas was enacted, each of such respective distributing company defendants, during the portion of said period it has been in existence, has been under the jurisdiction and control of the defendant Public Service Commission and its predecessors in office in the usual respects in which Public Service Commissions exercise such control. That the sales to said distributing company defendants constitute the great bulk of plaintiff's business [fol. 236] in the state of Kansas and in practically every instance such defendants have no other source of supply and cannot procure gas elsewhere and also this plaintiff cannot supplant its said customers with other customers for the reason, among others, that its said pipeline system has been built to serve these markets and it is economically prohibitive to lay pipelines to other distant markets even if such markets could be secured. That plaintiff's business could not be continued if it were deprived of the business of said distributing company defendants and in practically every instance the business of said distributing company defendants could not be continued unless they were permitted to purchase gas from plaintiff. That since the enactment of said public utility law as aforesaid and the various successive amendments thereto it has been the subject of litigation as to the extent and application of the powers of the defendant Public Service Commission, and its predecessors in office, which decisions have become and are an integral part of said public utility laws. That among such decisions so supplementing said law there is one by the United States Supreme Court squarely holding as against the predecessors in office of the defendant, Public Service Commission, that the business hereinbefore described and then conducted by a predecessor in title of this plaintiff was an interstate

business of such national concern as to be beyond the jurisdiction of the predecessors in office of the said Public Service Commission and another, by the Supreme Court of the State of Kansas that the present defendant, Public Service Commission, had no power of regulation over this plaintiff which said decisions are equally as integral a part of the public utility laws of the State of Kansas as the text of the law itself, which interpretation and application of said laws has in recent years been uniformly acquiesced in and [fol. 237] accepted by the defendant, Public Service Commission, until the happening of the things complained of herein.

XVII

That according to the usual established course of its business plaintiff has been accustomed to produce or purchase and transport from other states through its said integrated gas pipeline system and sell at wholesale a quantity of gas ranging approximately from a minimum of one hundred million cubic feet daily to a maximum of approximately three hundred thirty million cubic feet daily of natural gas. About 58% of such gas so sold was sold in Kansas and most of that which was sold to domestic consumers in Kansas was and is sold to the distributing company defendants herein. That the prices stipulated in the various contracts with said distributing company defendants vary somewhat because of varying circumstances and conditions but the weighted average price agreed to be paid by said distributing company defendants for domestic gas is 39.5 cents per thousand cubic feet, the maximum price charged to any distributing company defendant being 40 cents per thousand cubic feet. That in each instance the contract was oral and it was agreed and understood that it was to remain in force and effect until changed by agreement of the parties. That said maximum price of 40 cents per thousand cubic feet is the price that was fixed as a reasonable price by the predecessors in office of said defendant Commission for domestic gas in 1923 and is the same price which distributing companies in the state of Kansas entirely unrelated to plaintiff have since paid and still pay to plaintiff and same is a fair and reasonable price for same and the amount necessary for plaintiff to receive in order

[fol. 238] to maintain its said pipeline system and business and produce a moderate and reasonable profit therefrom.

## XVIII

That frequently while plaintiff was so conducting its said business it has been compelled to largely expand its facilities to reach other population centers and to render more dependable its service to the distributing companies in the cities which its said pipeline system already reached and as incidental thereto it has been confronted with heavy financing undertakings, construction and managerial problems. That constantly during said period plaintiff has had the advantage of the advice, cooperation, assistance and supervision of many long and widely experienced experts in said respective lines employed by Henry L. Doherty & Company acting as fiscal agent of Cities Service Company, and located in the chief and most advantageous money center of the world, which connection has been extremely valuable and profitable to this plaintiff and has saved it large sums of money as interest and because of its being enabled with such expert assistance to do things most efficiently and to avoid expensive blunders that companies not endowed with such expert and experienced assistance would naturally make in conducting complicated affairs with ordinary employees. That under written contract with said Henry L. Doherty & Company plaintiff has agreed to pay and has in the past paid to said Henry L. Doherty & Company as fiscal agent of said Cities Service Company one and three-fourths per cent of its gross annual income from sales of natural gas to persons and companies other than the distributing company defendants herein and other affiliated companies, such percentage being calculated to recompense [fol. 239] merely said Henry L. Doherty & Company for the actual cost to it of furnishing said services. That said amount averaged over said period has rendered no profit to said Henry L. Doherty & Company but in the aggregate has actually failed to pay to it the actual cost of furnishing said services, and over a period of years said contract has been very advantageous and profitable to this plaintiff. Furthermore during said period since 1927 plaintiff has been able to take from its gas wells located in the Panhandle Field of Texas gas to fill a great portion of its re-

quirements which it produced at small cost to it and at all such times was permitted by the laws and rules of the state of Texas to take from each well a maximum of twenty-five percent of the open flow of such well. That by reason of said advantageous connections and its ability to draw so largely from the Texas Panhandle Field its experience has been fairly profitable and during the year ending with the approximate date of the order hereinafter complained of it made a net profit after depreciation and depletion of approximately five million dollars out of its said business, which constituted a net profit of only about five percent on the value of all the properties owned by it and enlisted in its business. That its gross income for said period was approximately fourteen million dollars and the reduction of its gross income by twenty-five percent would reduce its net income on its investment and the fair value of its properties to approximately two (2%) percent, under which circumstances plaintiff could not continue to operate. That if a reduction be made of its price for domestic gas in Kansas it will be compelled, in order to avoid offensive discrimination and destructive reprisals by other states or their inhabitants, to reduce its prices for such gas in all other states in which it operates.

[fol. 240]

XIX

That while plaintiff was so conducting its well established business in the ordinary way as aforesaid the said defendant The Public Service Commission of the State of Kansas about July 2nd, 1931, and pretending to act under Chapter 239 of the Session Laws of the State of Kansas for 1931, which in substance attempts to confer on said defendant Commission the power to compel holding companies of and corporations affiliated with public utility corporations operating in the State of Kansas to furnish information to it and providing that no management or similar contract of such public utility corporation with an affiliated corporation shall be effective until filed with said Commission, and further providing in substance that upon a proper hearing if such contract be found not to be in the public interest such Commission would be authorized to disapprove such contract, and further providing that "in ascertaining the reasonableness of a rate or charge made by a public utility"

no charge made by a holding or affiliated company shall be given consideration in determining such rate of such public utility to the public unless a showing be made by the utility affected by the charge as to the actual cost to the holding or affiliated company, such showing to consist of an itemized statement furnished by said utility setting out the items, did wrongfully cause to be served upon all of plaintiff's aforesaid customers in the State of Kansas that were directly or indirectly affiliated with it notices of a hearing, a copy of one typical of all of which is hereto attached, marked Exhibit "L" and made a part hereof. That thereafter for more than one year said Commission intermittently held hearings, purporting to be under said notices and wrongfully and without authority of law considered the [fol. 241] aforesaid contract of this plaintiff, which was not a party nor a public utility under the jurisdiction of said defendant Commission, with Henry L. Doherty & Company as fiscal agent of Cities Service Company to pay to it one and three-fourths per cent of its gross receipts from sales of gas to persons and companies not affiliated with plaintiff, and assumed to abrogate and repudiate as a portion of plaintiff's property rights the said contract, whereas neither the statute aforementioned purporting to cover germane matters nor any other statute of the State of Kansas confer upon said defendant Commission the authority or jurisdiction to consider, affect, reject or annul such a contract, it not being one made with a public utility under its jurisdiction. That said defendant Commission, pretending to act under said notice and without ordering or instituting a rate hearing upon any of said distributing company defendants or any other customer of plaintiff to determine the ultimate charge of said customers to the public, wrongfully and without authority of law or any jurisdiction over the subject attempted to impose indirectly upon plaintiff that regulation of plaintiff's business, the direct exercise of which said laws as construed and supplemented by said decisions prohibited to it, and attempted to supersede and supplant the business discretion, judgment and decision of the Board of Directors and officers of plaintiff and of its said affiliated customers, respectively, by unlawfully dictating the purchase price of gas, which was only one element of the ultimate composite sum representing the ultimate charge of

said affiliated customers to the public, thereby depriving this plaintiff and its said customers of the freedom of contract and usurping the power of the Congress of the United States to regulate commerce among the states and depriving plaintiff's said customers, and in necessary effect de- [fol. 242] priving plaintiff, of all corporate autonomy by prohibiting them and it from proportioning the elements entering into the ultimate charge to consumers as the business judgment of said respective customers should dictate, which power said customers legally have and are entitled to exercise constantly so long as they do not exceed such reasonable ultimate rate as the Commission may legally impose, whereas said defendant Commission has no power to consider such things except in a rate hearing, and even in such hearing has no power to determine what a public utility under its jurisdiction shall pay for gas or any other element of its business, but has only the power, and only in such a hearing, to determine and dictate upon proper evidence the ultimate charge of said public utilities to their respective customers. That in such hearing said defendant Commission expressly refused to plaintiff's said customers upon their direct application therefor the right to show, respectively, their present financial experiences so that said defendant Commission might determine for them respectively and appropriate rates to be charged to their customers for the natural gas sold by said customers. That said defendant Commission further wrongfully refused to take or consider plaintiff's well established business as it was currently going forward in the accustomed way or had existed in the recent past or to consider the actual value of the properties acquired for and enlisted in said enterprise, but undertook to revamp the business and select properties of plaintiff, to be considered for the purpose of ascertaining whether plaintiff was earning a reasonable return upon its investment, according to their caprice or inexperienced notions as to what properties only plaintiff ought to own or enlist in such enterprise, and wrongfully undertook to repudiate the aforesaid management contract, not even allowing as an item of expense the quantum meruit of such services, en- [fol. 243] tirely failing and refusing at all times to take the plaintiff, its business, its contracts and profits as they historically existed and were found; but instead insisted upon

considering plaintiff as they pretended to conceive it, its business, its contracts and profits should have been, thereby substituting its business judgment for the business judgment of the plaintiff, although said defendant Commission in substance and effect found that plaintiff was conducting its business in good faith and had wisely acquired and owned many thousand acres of valuable gas lands, which said Commission refused to consider as an integral part of plaintiff's investment in its business or to use as a basis for calculating the percentage of its profits.

XX

That instead of taking plaintiff historically as it found it and attempting to ascertain the actual cost to plaintiff of the commodities it was selling and the service it was furnishing to said distributing companies, said defendant Commission in direct violation of said Chapter 239 and in direct violation of the provisions of the Federal Constitution prohibiting it from regulating interstate commerce, the impairment of contracts, the taking of property without due process of law, rejected the itemized statements of the distributing company defendants herein, showing the cost of the gas and services furnished by plaintiff, without evidence questioning or refuting same, and, as if it had regulatory power over plaintiff, wrongfully and without jurisdiction so to do assumed to take a valuation made by persons selected by said Commission of plaintiff's properties not only in the State of Kansas but also lying in [fol. 244] the States of Texas, Oklahoma, Nebraska and Missouri, where said Commission had no jurisdiction whatever, to determine its reproduction cost new depreciated at the nadir of the trough of the deepest depression the world has ever known, when cost prices were radically below the necessary amounts actually paid by plaintiff and its predecessors in title for construction of its said pipeline system. By this process said defendant Commission eliminated millions of dollars of actual cost and expenditures made by this plaintiff in the lawful conduct of its business; and that by so doing it also excluded from its alleged rate base millions of dollars' worth of leases, thereby in effect confiscating the property of this plaintiff to the extent of such elimination. That plaintiff has no other busi-

ness and unless it is permitted to earn from this business upon all of its property it will be obliged to surrender the leases excluded by said defendant Commission in arriving at its pretended rate base and if the proceeding of said Commission is permitted to stand it will work a confiscation of plaintiff's property to the extent of millions of dollars.

XXI

That in substance the said orders (Exhibits "H" and "I" attached hereto) issued by said defendant Public Service Commission on August 31, 1932, against each and all of the distributing company defendants herein and all other customers of plaintiff in the State of Kansas that are affiliated to it, is that said distributng companies are prohibited from entering upon their books any greater charge for gas sold to them by this plaintiff for domestic use than 30 cents per thousand cubic feet, and from considering in their sales price to their customers any larger amount than said sum, and, contrary to the statutes of Kansas providing [fol. 245] that the orders of the Commission should become effective thirty days after the date of their entry, said defendant Commission directed that its order should become effective the next day following its date, or September 1, 1932. That if said order be permitted to stand and be given force and effect it will prevent said customers of plaintiff from paying to it more than 30 cents per thousand cubic feet for gas sold for domestic purposes, and if said plaintiff is thus wrongfully compelled to sell its product at a price that will constantly cause it loss the inevitable and speedy result will be that its assets will be depleted and its properties destroyed and if on the other hand plaintiff's said customers pay to it the said contract price for domestic gas and are prevented from collecting from their respective consumers more than a rate based upon a purchase price of 30 cents per thousand cubic feet the assets of said customers will be depleted, their respective businesses destroyed and they will become unable to purchase any gas from plaintiff. In either event the necessary effect and operation of said orders will be the destruction of plaintiff's business and the confiscation of its property. That to so destroy plaintiff's said markets as aforesaid by making the orders upon its customers who are necessary

to the continuance of its business will as effectually destroy plaintiff's business and confiscate its property as to make the orders directly upon plaintiff prohibiting it from selling its product for domestic use at more than 30 cents per thousand cubic feet.

XXII

Plaintiff further says that each and all of the distributing company defendants are interested in the subject matter of this controversy and will be compelled to breach their respective gas purchase contracts with the plaintiff [fol. 246] if said orders of said defendant Public Service Commission are permitted to stand, and are proper parties for a complete determination of all the matters involved herein.

XXIII

That the said orders complained of herein violate plaintiff's rights under the Federal Constitution and are in direct contravention of the following provisions of the Constitution of the United States: Clause 1, Section 10, Article 1 of the Constitution of the United States forbidding any state from passing a law impairing the obligation of contracts; the Fourteenth Amendment to the Constitution of the United States forbidding the taking of property without due process of law and the denial of the equal protection of the laws, and Clause 3, Section 8, Article 1 of the Constitution of the United States vesting exclusively in Congress the power to regulate commerce among the states.

XXIV

That the said Public Service Commission, for the purpose of intimidating and coercing this plaintiff and the defendant distributing companies, and by means of such intimidation and coercion preventing the said plaintiff and said defendant distributing companies from seeking any review of the said order of the Public Service Commission (Exhibit "H" attached hereto) in the state courts of Kansas and from seeking any relief by way of injunction or otherwise in this or other courts of the United States, and

by means of such intimidation or coercion of compelling the plaintiff and the defendant distributing companies to acquiesce in and comply with the said order, plans and threatens illegally to institute proceedings in the state [fol. 247] courts of Kansas against the defendant distributing companies in an attempt and with the avowed purpose of having receivers appointed for the defendant distributing companies and through such receivers, if appointed, to have the defendant distributing companies accept and acquiesce in said order and by means of the appointment of such receivers to frustrate and prevent the plaintiff and the defendant distributing companies from seeking or obtaining a review of said order or testing its validity in either the state courts of Kansas of this Court and by such groundless procedure unlawfully to coerce and destroy the plaintiff's customers and prevent such customers of the plaintiff from carrying out or performing their respective contracts with the plaintiff for the purchase of gas, and unlawfully, and by indirect means, to attack and destroy the efficiency, credit and property of this plaintiff and of the defendant distributing companies. That such threatened action, recommendation or purpose on the part of the said Public Service Commission is and would be beyond its power and authority and contrary to the statutes of the State of Kansas, but notwithstanding this it has recommended such procedure to the Governor of Kansas, who in turn has ordered the defendant Attorney General to bring such actions and he has publicly stated that he would speedily do so. That if such proceeding be instituted, irrespective of its final outcome, it would cause this plaintiff irreparable damage and deprive it of its property and contract rights without due process of law and deny to it the equal protection of the laws in violation of the Fourteenth Amendment to the Constitution of the United States, and would impair the obligation of its existing contracts contrary to Section 10 of Article 1 of the Constitution of the United States.

[fol. 248] XXV

Unless the Public Service Commission of the State of Kansas, defendants herein, are restrained and enjoined as herein prayed, as plaintiff believes and so alleges, plain-

tiff's customers will be induced and caused to resist and refuse payment of any charges and rates for natural gas other than those that may result from the enforcement of the said order of the said Commission (Exhibits "H" and "I" hereto attached). Because of the nature of plaintiff's business it has no practical way to enforce the collection of its charges. By cutting off or refusing service for default in the payment of bills rendered, plaintiff's customers, as plaintiff believes and so alleges, will institute large numbers of suits in various jurisdictions throughout the State of Kansas and elsewhere to restrain the plaintiff from cutting off and denying service, and for damages, and also if plaintiff attempts to collect its bills through litigation, such litigation will entail a large number of law suits in various jurisdictions, and therefore plaintiff, in any case, will be subjected to an endless multiplicity of suits. That the issues which would be presented in each such suit are presented and should and will be decided in this action.

XXVI

That Union Public Service Company is a proper but not necessary party and is not made a party for the reason that it cannot be made a party without ousting the jurisdiction on one phase of the case. That plaintiff has no plain, speedy or adequate remedy at law.

Wherefore, plaintiff prays:

1st. That the rate, charge and price of 30c per thousand cubic feet for the defendant distributing companies to pay [fol. 249] to the plaintiff for main line town border domestic gas as prescribed in the orders of the Public Service Commission dated August 31, 1932 (Exhibit "H" attached hereto) be decreed to be confiscatory of the property of this plaintiff, in violation of the Constitution of the United States, and said order imposing the same to be void.

2nd. That The Public Service Commission of the State of Kansas and said individual defendants composing same, and said defendant, Roland Boynton, Attorney General of the State of Kansas, and each of them, their attorneys, agents and employees, and all other persons be temporarily

and permanently restrained and enjoined from any attempt to enforce the said orders of said Public Service Commission or to compel the plaintiff, directly or indirectly, its officers, directors, agents and employees, to comply with, observe or put in force as of September 1, 1932, or comply with, observe or keep in force thereafter the rate, charge or price to the defendant distributing companies or any of them of 30c per thousand cubic feet for main line town border gas supplied to the defendant distributing companies or any of them, or to others, and from any attempt to compel plaintiff, its officers, directors, agents and employees, to comply with or recognize the said orders of the Public Service Commission of the State of Kansas, dated August 31, 1932, (Exhibits "H" and "I" attached hereto) or any other order of the said Public Service Commission, and from taking any steps or proceedings against the said distributing company defendants, their officers, directors, agents or employees, to enforce any penalties or any other remedy for disregarding the rates, charges and prices prescribed by the said orders of the Public Service Commission dated August 31, 1932, (Exhibits "H" and "I" at- [fol. 250] tached hereto) or any of the provisions or findings thereof.

3rd. That the defendant distributing companies and each of them, and all other persons, be temporarily and permanently restrained and enjoined from failing or refusing to carry out their respective agreements with plaintiff for the purchase of natural gas and from failing or refusing to pay to the plaintiff for natural gas received from the plaintiff at the town border of each of the various communities served by the defendant distributing companies respectively the rate, price or charge which each of the said defendant distributing companies has been and now is paying to the plaintiff for such gas, because of said orders or any other orders issued or to be issued out of, based upon or growing out of said proceeding, Docket No. 13127.

4th: That the defendant The Public Service Commission of the State of Kansas, and said individual defendants composing same, and said defendant Roland Boynton, Attorney General of the State of Kansas, and each of them, their officers, agents, servants, employees and attorneys

and those in active concert or participating with them be temporarily and permanently restrained and enjoined from any attempt to bring ouster, dissolution or receivership actions or proceedings against said distributing company defendants or any of them or any other customer of plaintiff in the State of Kansas affiliated with it, for the purpose of preventing disabling or impairing the ability of any or all of them from complying, or to comply, with their said respective contracts with plaintiff hereinbefore set out and from taking any steps that will directly or indirectly bring about or tend to cause such result.

[fol. 251] 5th. That the plaintiff have such other and further relief as may be equitable in the premises.

6th. That a writ of subpoena of the United States of America issue out of and under the seal of this Honorable Court, directed to and against the defendants herein and each of them as required by law, commanding them and each of them on a day certain to be named therein, and under a certain penalty, to appear and fully submit and make answer to this bill of complaint.

7th. That a hearing and determination shall be had herein by three judges as provided by Section 266 of the Judicial Code as amended, for a restraining order and an interlocutory injunction as hereinbefore prayed for, and upon the final hearing and determination upon the merits, and the rendition of final judgment herein, by the said statutory court of three, that a writ of permanent injunction be granted perpetually restraining and enjoining the defendants and each of them as hereinbefore prayed.

And this plaintiff will ever pray.

Cities Service Gas Company, by James W. Finley, Bartlesville, Okla.; R. E. Cullison, Bartlesville, Okla.; Charles A. Frueauff, New York City; Robert S. Sloan, New York City; Fred Robertson, Kansas City, Kan.; J. O. Emerson, Kansas City, Kan, Attorneys for Plaintiff.

[fol. 252] *Duly sworn to by James W. Finley. Jurat omitted in printing.*

Exhibit "A" to Bill of Complaint

Mr. Garver: I desire to make an opening statement to the Commission, and in order that there may be no misunderstanding I have written it.

If the Commission please, at the outset we must confess some uncertainty and confusion as to the nature of this proceeding; the purpose of the Commission; its jurisdiction and our duty. There has never before been anything of the kind attempted and there is no precedent to follow. For this reason and to avoid any uncertainty as to our contentions we have filed written appearances for the several respondents.

[fol. 253] We say the proceeding is unusual in that we have here joined in one order and involved in one hearing separate and distinct properties in some one hundred and eighty cities and communities. Some of these properties have heretofore been involved in separate rate hearings and such hearings as to one property have taken weeks. The rates of each system must of necessity be based on the value of its property and its financial experience. The statutes contemplate separate hearings and provide for a review by the courts on the record as to that property, the venue being determined by the location of the property. It would lead to the utmost confusion, would thwart the purposes of the statute and would jeopardize the statutory and consitutional rights of these several respondents should they be expected to submit to a joint hearing involving the valuation and financial experience of one hundred and eighty properties, none of which is, in any manner, concerned with any other property. We therefore enter this proceeding with the definite contention that it is not a rate case as to any particular property and involves no consideration of the reasonableness or unreasonableness of their rates.

The proceeding, as we recognize it, is an investigation of three particular contracts between companies associated through an ultimate common ownership of a control of their voting stock. These contracts are as follows:

First, the contract with Henry L. Doherty & Company under which 1¾ per cent of the gross earnings are paid to defray the expense, without profit, of services rendered by that organization.

Second, the contract under which the expense of the Gas Service Company is allocated to the several properties, being the expense, without profit, of services rendered by it. [fol. 254] The third is the price paid for gas by the several distributing companies at the city gate.

The first two matters are of slight importance notwithstanding the fact that they have been the subject of much criticism and tirades of abuse. In no rate case so far tried have they been a controlling consideration and they could have been excluded or included without affecting the result of those cases. In the last case involving these properties to be heard by this Commission, El Dorado, we informed the Commission that if not satisfied with the justice of the items they could be thrown out entirely. That is our position now, although we believe they are just and should be so accepted, as they have been so declared by the highest court of our state and by the District Court of the United States. Frankly it has not seemed to us either fair to us or respectful to the courts for this Commission to disregard those decisions and persist in its own contrary judgment. However, we will, in this proceeding, again lay before the Commission all the facts.

As to the city gate rate, the situation is not greatly different although of controlling importance. The existing rate has twice been held reasonable by the courts, including the highest court of this state. Within four months of the last adjudication this Commission dismissed the application of the Western Distributing Company for increased rates at El Dorado because the company declined to again relitigate that matter which the then representatives of this Commission solemnly agreed in open court should be considered as settled. It seemed to us most unfair in that proceeding, which was a hearing in one of twenty-two applications filed by The Western Distributing Company for twenty-two separate towns, some with less than one hundred meters, to expect the distributing company to put on [fol. 255] a complete rate case as to the pipe line. I then informed the Commission such a requirement was prohibitive on account of the expense involved and the smallness of the towns. That this is true is well demonstrated by the expense of this proceeding. At this time of extreme depression, when large industries throughout the country have been compelled to lay off men and cut wages to offset

their greatly reduced earnings in order to survive the crisis, and in the face of a demand of lower rates, we have, to date, in preparation for this proceeding, expended between one hundred fifty and two hundred thousand dollars and the hearing has just begun. This is more than the property at ElDorado ever has or ever will make under its present experience.

In coming before this Commission we do so doubtful of the legal rights of the Commission to compel us to incur this expense doubtful of the legal right to fix an interstate rate in view of many decisions of the United States Supreme Court to the contrary, but realizing a duty to the public to answer our accusers and make all facts public.

We trust this Commission will hear our evidence with open minds and give to us in some measure the benefit of an honesty of purpose. We have naturally been disturbed by articles that have appeared in the press, attributed to members of this body, from which, if true, it would appear the case has been prejudged and its issues determined against us in advance. If so, of course this proceeding is but a farce and an idle gesture. We hope, however, by our conduct in presenting it, to merit your fair and honest consideration.

The majority of this Commission is new to its duties, having taken office within the year. During such time as [fol. 256] the matter of gas rates has been of interest to such members a bitter controversy has existed between our companies and the Kansas City Star involving personal and private differences, and another with the Governor of this State, of a more political nature. Law suits have resulted and charges and counter charges have been made in court and out. It would not be unusual or unnatural if all this had formed a prejudice, consciously or otherwise, in the minds of the public and the minds of the members of this body. I am, therefore, asking that I be indulged in a short history of events that have preceded.

Most of the charges made against us are that we enjoy a monopoly. To the unthinking, monopoly means excess and unjustified profits.

* * * * * * *

Mr. Garver: I think your Commission, in order to give a fair consideration to this matter should know the way

we feel about it. By that I mean our organization, and my clients. There is no malice or animosity in this. I am only getting at this background, as we see it, and try to put yourselves in our position and view the case from that angle.

But this does not follow. At the time Cities Service Company entered the gas business in Kansas the then gas pipe lines enjoyed a perfect monopoly. There were no other companies and they had everything their own way. But they went broke; service failed utterly; the investors lost a large part of their investment; the bankrupt and disgraced properties were sold as is the property of all others who fail.

From the date these failures were purchased and collected into an orderly system service improved and in the past ten years has been such as was never known before [fol. 257] and concerning which there is no complaint now. When these lines were taken over there was no adequate supply of gas—no adequate appliances through which to utilize it. All was confusion as far as the gas business in Kansas was concerned. This has all been changed and to Mr. Doherty more than to any other man, is due the credit for bringing order out of confusion and for rendering service where none before existed.

It has never been the policy of Mr. Doherty to dictate to these properties from an office far distant from their customers, or to place in charge of them men of Wall Street training, unsympathetic with the people served, without understanding of their problems and actuated only by the thought of making money. H. O. Caster is the one now in charge of the natural gas division of Cities Service Company. Judge Caster is a product of a small Kansas town and was formerly attorney for this Commission. He was brought up not in luxury but privation—one of the common people of Kansas, and as much one of them now in his high position as when on the farm in years gone by. No man has ever questioned his word or doubted his integrity. He knows, better than any one else, whether things are right or wrong in Kansas gas rates. He has tried to tell the facts to Kansas officials many times. I doubt if any of them thought he lied but there was always so much political din his voice could not be heard above the tumult. Then there is Jim Finley, formerly one of your judges and

your senator, Sam Hawks, for many years your assistant attorney general; Major Strickler, formerly Chief Engineer of this Commission, myself and many others. Have all these men changed their characters with their employment and sold their birthright for a mess of pottage? I do not believe you have any such thought. As to these men [fol. 258] and myself, we are proud of what has been accomplished by our organization. We feel it has rendered a real service. It is hard for us to realize there is no appreciation of what has been done or to understand the existing criticism.

The rates now in effect are not our arbitrary pronouncements. They have each and all been fixed by either this Commission or by the courts, after repeated and exhaustive investigations and at an expense of many thousands of dollars. We see no reason why these repeated adjudications of our lawful tribunals should be treated with disrespect and in the face of them we should be charged with unlawful conduct. If our system of government is to continue our conduct in the future must be as it has been in the past. There is no other course open to us. When our rates are so established they should be accepted as is the decision of the courts in other matters and the orderly procedure of the courts should not be forgotten and the accusation made that such rates are the offspring of monopoly.

In fact, there is no such thing as monopoly in the gas business regardless of whether there be one company or many. Gas companies are merely merchants selling fuel in competition with other fuels. When the public can buy more comfort and satisfaction for a dollar spent for gas than a dollar spent for coal, oil or electricity, so long and no longer will that dollar be so spent. The competition was never so keen as now. Five years ago the several companies in this group, unable to meet this competition, were losing business steadily year by year. Their revenues were declining so alarmingly that to avoid absolute failure and inability to render service the sale of appliances was undertaken for the sole purpose of increasing the use of this fuel. The result was most satisfactory and the use of gas greatly increased thereby continuing in effect rates [fol. 259] which otherwise would have had to be raised

if the companies were to continue their existence. Now there is an attempt being made to deprive them of the only shield that can protect them against the inroads of their competitors. Instead of monopoly there is competition of the keenest character ever known to the industry.

From the small beginning which our companies made in the purchase of the old Kansas Natural pipe line, a complete, adequate and efficient system, as large as any in the world, has grown. It has not grown by itself nor by reason of earnings of the business. The present value of pipe lines and distribution systems in Texas, Oklahoma, Kansas and Missouri approximates the enormous sum of $150,000,000.00. On this we have never earned a fair return.

But the gas business is only a part of the Cities Service Companies' contribution to the prosperity of Kansas. At this time our affiliated companies have in Kansas 2500 employees, who provide the support for at least 10,000 citizens. The annual salaries and wages to these employees is approximately $3,769,000.00, all of which is spent in Kansas. In addition, our companies in 1930 paid $2,000,000.00 for lease rentals and purchases which went to Kansas farm owners; $1,178,750.00 to Kansas labor; $688,600 to Kansas drilling contractors, most of which went to Kansas labor; $1,148,008.00 was paid to Kansas well-owners for oil; $1,130,000.00 to Kansas well-owners for gas; $1,114,000.00 for 1930 taxes; $1,298,761.00 by gas distribution companies—and other expenditures, the figures for which are not available.

These several known items aggregate $12,327,119.00 spent in Kansas in 1930, more than $1,000,000.00 a month. What other organization in Kansas contributes $1,000,000.00 a month to its prosperity? Our organization feels [fol. 260] that it has done as much for the state as any other organization and fails to understand why it is now singled out for attack.

The intent of Cities Service Company in the beginning was to confine its activities to the pipe line end of the business, leaving the distributing companies in the hands of their then owners entirely unassociated with our organization. Prior to the year 1924 only a few destributing companies of minor importance were owned directly or indirectly by Cities Service Company, the same consisting of the towns in The Western Distributing Company group,

of which El Dorado was the only city of importance. The large markets, such as the two Kansas cities, Wichita, Newton, Hutchinson and Topeka, were owned by corporations unfriendly to the pipeline ownership and had been antagonists in litigation with it for the preceding ten years. There was no co operation on the part of the distributing companies in building up a market which would justify the millions of dollars in additional pipe line investment which was required, not to reach new markets, but to give adequate service to customers then connected. The distributing companies were making no effort to solicit business, were expressly discouraging the use of gas for house heating or industrial purposes and were all experiencing declines in the volume of gas sold and in earnings. In the opinion of the officials of the company, responsible for adequacy of service by the pipe line, the situation was such as to require ownership of the distributing companies in order to assure a market which would justify a greatly increased investment and which was necessary in order to give proper and adequate service to the consumers.

Purchases were made of the distributing company at Topeka, then in the hands of a receiver, and of the dis- [fol. 261] tributing companies at Wichita, Hutchinson, Newton, Pittsburg, the two Kansas Cities, and Union Public Service Company, with distribution systems in some twenty five towns and communities in Kansas, the principal cities being Parsons and Ottawa.

The Gas Service Company was organized in order that experienced and competent men might be placed in close touch with the operation of these properties, it being believed that more could be accomplished by the personal contact of a local organization acting in conjunction and cooperation with the New York office than by that office alone, far distant from the communities' problems.

The agitation against gas companies and the cry of unfairness began at about this time, no doubt due to the fact that the rates fixed in franchises granted by the several cities in the period from 1906 to 1910 had all been set aside as insufficient and confiscatory at the end of years of bitter and expensive litigation and all rates to consumers has been substantially increased.

At the time the properties at Wichita, Hutchinson and Newton were purchased none of them were making oper-

ating expenses and the Kansas Gas & Electric Company had cases pending before the Kansas Commission asking for increases in rates, all of which cases were being bitterly opposed by the several cities. Not desiring to enter said cities as contestants in existing controversies and desiring an opportunity to see what could be done under existing rates; notwithstanding the disastrous experience of its predecessors, the new owners dismissed all said cases then under advisement by the Commission, briefed and ready for decision. The dismissal of these cases did not have the hoped for result and did not lessen the growing agitation.

[fol. 262] Rate cases soon developed on complaints filed by the cities of Wichita, Hutchinson and Newton which resulted in numerous hearings before this Commission, numerous orders and numerous appeals to the courts by the companies involved, the several companies fighting only for a fair return, and contending continually for rates adequate to enable them to render service. Orders issued by the Commission were set aside by the courts and within a few months new orders would be issued by the Commission entirely at variance with the court's decisions. In two instances the Commission did not even wait for appeals from their orders to be determined by the courts in the usual and statutory manner but started new cases involving the same matters for no other purpose than to have the utilities still before them should pending litigation be determined adversely to it.

In addition to rate litigation the several companies in this group were also forced to defend against suits for injunction, suits for receivers, suits to cancel franchises and other litigation, the main purpose of which was to annoy and harass them. All of this litigation was decided in favor of the companies but such decisions, far from being respected, seemed only to have increased the activities of the enemies of our organization and driven them to further and more violent attacks.

As we view this proceeding, the principal issue is as to the reasonableness of the present city gate rate. This rate was established by this Commission in 1923 at a time when the pipe line company submitted itself to the jurisdiction of the Commission and sought its aid in procuring adequate rates. In its order fixing the forty cent city gate

rate this Commission found that the pipe line company in 1923, on the lowest valuation submitted by any of the witnesses, including the Commission's own engineer, was [fol. 263] earning, for return and depreciation, under a thirty-five cent rate, less than two per cent, on such value. Since that time millions of dollars have been spent in the extension of lines to Oklahoma and Texas not for the purpose of seeking additional markets or procuring additional customers but for the purpose of rendering service to the customers then on the system. The valuation which in 1923 was approximately $50,000,000.00, has risen to approximately $100,000,000.00. That money was not procured from the earnings of the system but new and additional capital was required to be advanced by the owners of the property. In the period from 1923 to the present time more money has been invested in additions and betterments than the property has produced for its owners and, as far as the owners of the property are concerned, not one cent has been received in dividends which has not been put back in the property for the benefit of the customers connected therewith. Our organization is likewise unable to understand why its conduct in this regard should not entitle it to some degree of appreciation and approbation rather than continued criticism.

The question in which the Commission should now be interested, and the only issue which we now recognize in this proceeding, as far as the city gate rate is concerned, is as to whether or not the earnings of the Cities Service Gas Company, under the existing city gate rate, are more than a fair return on the fair value of its property. We will show this value, we believe, to the satisfaction of any unprejudiced mind, not only by our own witnesses but by disinterested witnesses of national standing and reputation. In order that the Commission might have in advance a fair opportunity to itself determine the value of this property we have furnished to it not only all the information that has been requested but have granted [fol. 264] access to the books of the respective companies whenever requested and have furnished, without cost to the Commission or its representatives, the cooperation and services of the employees of the respective companies. If there be any question as to that we will leave its answer to Mr. Black and Mr. Montgomery, the engineer and ac-

countant employed by this Commission for the purposes of this proceeding.

On whatever value is shown to exist, the pipe line company is entitled to a fair return. It asks nothing more. At this time it is not receiving such return.

There has always been a tendency on the part of former Commissions to assume the role of operators of utility properties and to substitute their judgment in lieu of the judgment of those entrusted by the owners with this responsibility. This tendency, however, has never been to assume any responsibility for an adequate supply of gas. Over a long period of years the companies have never received any help in this responsibility from regulatory bodies but have always been greatly hampered in their efforts to faithfully discharge their duty by criticism of their judgment and questioning of the reasonableness of their expenditures. The $150,000,000 invested in pipe lines and distribution systems and the $30,000,000 invested by our customers in gas using appliances would be practically lost were it not for an adequate supply of gas at all times, not the present only but indefinitely in the future. Without gas, pipe lines and gas burning appliances become mere junk with no value other than as such. The burden of shouldering this responsibility is no light one and should not be lightly considered either by the public or this Commission.

History has the habit of repeating itself. In the beginning, certain operators thought that gas could be sold at [fol. 265] cheap rates through single barrelled pipe lines built to local fields. When such fields failed the projects failed, the investors lost their money and the public lost service. There always have been and are now those who refuse to profit by experience and who believe, as did the original promoters of the old Kansas Natural, that its original dream can yet be realized. Those experienced in the industry believe that as to all such projects history will again repeat itself.

We know we have an adequate supply of gas for our customers' needs. We do not know that others have. We know we have a system of not one but many lines, not connected to one but many fields. We believe the needs of our customers have been safeguarded by us to the utmost and that we have faithfully performed our duty as to

them. Furthermore, we believe our customers, as a whole, are satisfied both as to service and rates. We know from experience they would prefer present service and present rates to the former inadequate service at lower rates. We respectfully decline to voluntarily do anything to cripple our ability to continue such service; nevertheless we recognize now and always that we are entitled only to a fair return on the fair value of our property. We ask that now nothing more.

* * * * * * * *

Mr. Stone: Now, if the Commission please, the last paragraph of the citation issued by the Commission contains this statement: "It is further by the Commission ordered: That each of the above named respondents appear on the abovementioned date to give to the Commission such information as they may desire on their own behalf, and as may be required by the Commission, in behalf of said investigation, and to show cause why such holding company contracts, or service or commodity charges, should they be [fol. 266] found to be unreasonable should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers." Now that paragraph, your honors, seems to contemplate that should you find forty cents to be too high at the city gate it should be reduced say to thirty five cents, or thirty cents, that that reduction of five or ten cents should be immediately adjusted as to each distributing company without any separate hearing as to the needs and requirements of that particular company.

* * * * * * * *

Mr. Stone: Our understanding was that the Commission contemplated proceeding then to make such adjustment without any hearing, and that is why we have filed these appearances as to each company, and I will read it so you may understand our position. Maybe there is no difference.

* * * * * * *

Mr. Stone: After stating the appearance, we say:

"Said respondent hereby expressly limits its appearance and appears specially for said purposes and said purposes

only hereby expressly objecting to any consideration by this Commission in this proceeding of the reasonableness or unreasonableness of its existing rates or any attempt to change the same by reason of any findings which this Commission may make in respect to said contracts from the evidence introduced herein and expressly denying the jurisdiction of the Commission to consider in this proceeding any issue as to the value of respondent's property, the adequacy or inadequacy of its earnings or the reasonableness or unreasonableness of its rates for the following reasons:

"1. That the Commission has no jurisdiction, power or [fol. 267] authority, under the laws of the State of Kansas, to proceed against utilities generally in one joint proceeding and to compel one utility to have joined with it others with which it has nothing in common.

"2. That this respondent owns and operates a public utility only in the city of Topeka, Kansas, and its immediate environs and its rates are, by law, required to be determined with respect to the value of its property used and useful in rendering its public service and without regard to the value of the properties of the other utilities joined herein.

"3. That the other parties respondent to this proceeding are improperly joined with the respondent and are not necessary or proper parties as far as any proceeding against this respondent is concerned which involves a consideration of its rates.

"4. That each public utility and each respondent herein as to each property which it operates is entitled under the law, to a full, complete and separate hearing as to each such city or community and the rates as to each such city or community must be considered by this Commission separate and apart and without regard to the property or rates of any other utility.

"5. That it will be impossible, in this proceeding, for any utility to make a record covering proceedings affecting it without including therein proceedings had concerning other utilities and impossible for such utility to avail itself of the right of appeal or review provided by law.

"6. That each utility respondent herein is deprived of the right to conduct its cause according to its independent judgment and in a legal and orderly manner and to avail itself of the rights granted and guaranteed by the Constitution and Laws of the United States and of the State of Kansas.

"7. That the existing rates of this respondent are inadequate, unremunerative and confiscatory in that they do not enable respondent to earn a fair return for all purposes on the fair value of its property and that no change in such rates can lawfully be made without affording respondent an opportunity to present all pertinent facts relating to the value of its property and its financial experience, which opportunity cannot be adequately afforded in this proceeding wherein respondent is joined with utilities operating in some one hundred and eighty towns and communities, the rates for each of which must be determined by considerations entirely independent of every other property."

[fol. 268] EXHIBIT "H" TO BILL OF COMPLAINT

Application for rehearing of The Arkansas Valley Gas Company omitted here, being identical with Exhibit "D" on behalf of The Wichita Gas Company, on page 43 of this record, except verification as follows:

STATE OF MISSOURI,
Jackson County, ss:

Robt. D. Garver, of lawful age, being first duly sworn, says that he is Vice-President of the respondent company filing the foregoing application for rehearing; that he has read over and knows the contents thereof and that the statements of fact therein alleged, and particularly the allegations of fact in paragraph 39 as to the earnings of Cities Service Gas Company for the year ending June 30th, 1932, are true.

Subscribed and sworn to before me this 29th day of July, 1932. My commission expires June 14th, 1934. ——, Notary Public.

[fol. 269] Exhibit "C" to Bill of Complaint

Before the Public Service Commission for the State of Kansas

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company.

Part A. Wichita Gas Company, Wichita, Kans.;
B. Hutchinson Gas Company, Hutchinson, Kans.;
C. Newton Gas Company, Newton, Kans.;
D. Pittsburg Gas Company, Pittsburg, Kans.;
E. Capital Gas and Electric Company, Topeka, Kans.;
F. Wyandotte County Gas Company, Kansas City, Kans.;
G. Arkansas Valley Gas Company, Arkansas City, Kans.;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 Towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kan.;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.;
Respondents

[fol. 270] Order for Information in Support of Application for Rehearing

Now on the 1st day of August, 1932, the Commission having before it for consideration the application of the above named respondents for rehearing in the above entitled cause finds:

That in order to enable the Commission to give proper consideration to the application for a rehearing the respondents in support of paragraph 39 of their application should submit to the Commission a complete earning and expense statement for the year ending June 30, 1932.

The Commission further finds that such earning and expense statement should show in detail all the earnings

of the Cities Service Gas Company for the year ending June 30, 1932, and all expense for the same period.

The Commission further finds that information should be included showing to the Commission loss in revenue due to reductions in the price of gas sold by the Cities Service Gas Company, amount paid to Henry L. Doherty & Co. for the year ending June 30, 1932, and what adjustment was made for construction credit if any.

The Commission further finds that the earning and expense statement should be submitted to the Commission on or before the 4th day of August, 1932.

It is, therefore, by the Commission ordered:

That the Respondents submit to the Commission on or before August 4, 1932, a comp. te earning and expense statement for the Cities Service Gas Company covering [fol. 271] the year ending June 30, 1932, in accordance with the findings above set forth.

By the Commission it is so ordered.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

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EXHIBIT "D" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Comes now The Pittsburg Gas Company, one of the respondents in the above entitled proceeding, and for its answer to the order of said Commission issued August 1st, 1932, and served upon one of its attorneys at approximately four P. M. on said date, and without recognizing the jurisdiction of the Commission to issue said order, or waiving the right to contest its validity, says:

[fol. 272] 1

That under the Statutes of the State of Kansas the proceedings before said Commission were closed by the is-

suance of its order of July 20th, 1932, and the Commission is without jurisdiction or authority to reopen same for the consideration of further evidence other than by granting respondent's application for a rehearing.

2

That respondent, under the Statutes of the State of Kansas, is entitled to have all evidence introduced by it made a part of the record of said proceedings in such manner that the same may be certified for the purposes of review by the courts, which right it will be denied if the procedure contemplated by said order of August 1st, 1932, is complied with.

3

That the application for a rehearing filed by respondent herein is part of the proceedings for review provided by the Statutes of the State of Kansas, and that Section 6 of Chapter 220, Laws of 1929, expressly prohibits the introduction of the evidence required by the Commission in its order of August 1st, 1932, or any other evidence, and said order of August 1st, 1932, is beyond the jurisdiction or power of the Commission and void.

4

That in said paragraph 39 of its application for a rehearing filed herein on July 30th, 1932, it asked for a rehearing for the reason that conditions had materially changed from those existing at the time of the several hear- [fol. 273] ings herein and that the experience of the Cities Service Gas Company for the year ending June 30th, 1932, was available and would show the ultimate facts set out in said paragraph 39 of said application for a rehearing, which facts are now apparent from an examination of the books of the said Cities Service Gas Company; that in respect to such changed conditions and the said experience of the said Cities Service Gas Company this respondent is entitled to a full and complete hearing and opportunity to present its evidence in the orderly manner contemplated by the Statutes of the State of Kansas and should not and cannot be required to limit its said hearing to the intro-

duction of one exhibit without opportunity to explain the same or in any manner supplement the information asked for by said Commission in said order of August 1st, 1932; that the true situation cannot be presented by any such exhibit even if it were physically possible to prepare the same in the time allowed in said order or within the time allowed by Statute for the consideration of said application and that respondent is unwilling to submit its case in that manner.

5

That even assuming the validity of said order of August 1st, 1932, the engineers and accountants, employed by respondent for the purpose of presenting its evidence and exhibits in said hearings before said Commission and who are familiar with the books and records of the Cities Service Gas Company, are not immediately available and, as respondent is informed and believes, even if present and ready to start the preparation of such an exhibit as is requested by the Commission, could not possibly complete the same in the unreasonably short time allowed by the Commission for that purpose or within the time allowed by [fol. 274] Statute for the consideration of said application for rehearing.

6

That if a rehearing is granted as applied for respondent will show that the amount paid to Henry L. Doherty & Company for the year ending June 30th, 1932, was approximately $52,000.00, representing 1¾ per cent of gross revenues from sales of gas to unaffiliated purchasers, which is a proper charge to the operating expenses of said Cities Service Gas Company for the reason that the prior action of said Commission in disallowing that payment as to the respondent companies was based on the assumption that the services of Henry L. Doherty & Company were duplicated by the services rendered by The Gas Service Company and the fact that respondents were affiliated with Cities Service Company whereas The Gas Service Company renders no services whatever for the Cities Service Gas Company and no possibility of duplication exists and the sales on which such payment is computed are to unaffiliated purchasers exclusively; that even if said item is

eliminated the earnings of the said Cities Service Gas Company would still fall approximately $1,200,000.00 short of a reasonable return had the rate established by said Commission in said order of July 20th, 1932, been in effect and applied to the business transacted by said company for said year ending June 30th, 1932, even if computed upon the Commission's own rate base and the Commission's own rate of return and replacement reserves, all of which is a part of the allowing respondent desires to make on rehearing.

[fol. 275] 7

That if a rehearing is granted respondent will show that during the year ending June 30th, 1932, the price charged by said Cities Service Gas Company to respondents for gas for domestic purposes at the city gates of their respective cities was the same as the price charged during the periods under consideration by the Commission in the previous hearings had herein and no part of the reduction in earnings shown by the experience for the year ending June 30th, 1932, as compared with the earnings for the periods under consideration by the Commission in previous hearings, was due to any such reduction in the city gate rates.

8

It is impossible for respondent to inform the Commission at this time the exact amount of any adjustment for construction credits made during the year ending June 30th, 1932, due to lack of time and opportunity to audit the books of said company for said purpose, but, on rehearing, will show that there was a construction credit of approximately $42,000.00 and that said adjustment was taken into consideration in arriving at the net earnings of $7,865,110.82, as alleged in paragraph 39 of said application for rehearing, and that in arriving at said figure all proper adjustments have been made.

9

Respondent further states that it is impossible to determine whether any part of the decreased earnings of the Cities Service Gas Company was due to a reduction in the price charged for industrial gas without a detailed analysis of every contract of the Cities Service Gas Company and

[fol. 276] of the several respondents herein covering the sale of industrial gas, which detailed analysis it is impossible to make in the time allowed by said Commission or in the time allowed by Statute for the consideration of said application for rehearing.

Wherefore respondent respectfully prays that the rehearing, as applied for, be granted and that it be granted an opportunity to show, in the manner contemplated by the Statutes of the State of Kansas, the several matters alleged in its said application for rehearing.

The Pittsburg Gas Company, by ———, Attorneys.

State of Missouri,
County of Jackson, ss:

H. L. Eastman, of lawful age, being first duly sworn, says that he is the same H. L. Eastman who testified in the hearings had herein as to the valuation and financial experience of the Cities Service Gas Company; that he has personally examined the books of said company for the purpose of ascertaining its financial experience for the year ending June 30th, 1932; that he has read over and knows the contents of the foregoing instrument and that the allegations of fact therein are true.

———

Subscribed and sworn to before me this 3rd day of August, 1932. My commission expires June 14th, 1934. ———, Notary Public.

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[fol. 277] Exhibit "E" to Bill of Complaint

Order granting a rehearing omitted here, being identical with Exhibit "E" on page 65 of this record.

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Exhibit "F" to Bill of Complaint

Respondents offer to show by the witness A. W. Ambrose that he is Vice President and Assistant General Manager of the Cities Service Gas Company; that he has been with

said Company since the year 1923; that prior thereto he was Chief Petroleum Technologist of the Bureau of Mines of the United States Government; that he is familiar with the gas reserves of Cities Service Gas Company, most of which were purchased under his direction and supervision; that in his opinion as an officer of said company they are all necessary in order to guarantee service to the consumers on said system; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas panhandle field was 1,263,000,000 feet per day of which only [fol. 278] 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oils, or blown in the air and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that said Commission now has under consideration an order limiting all takes from wells to five (5%) per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,267 acres allowed by this Commission will be wholly inadequate for even the coming winter, and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commission, service will fail; that under present practices in Texas the owners or approximately ten (10%) per cent of the leases are producing approximately eighty two (82%) per cent of the gas, none of which is connected to pipe lines or used by them; that such practices have reduced rock pressure in the Borger territory from the original 430 pounds to less than 50 pounds; that gas in the area including the 71,267 acres allowed by this Commission is migrating to the low pressure Borger area; that the reserves of gas under said 71,267 acres are being thus constantly depleted and are not available to the Cities Service Gas Company as assumed by this Commission; that in its computation of proper reserves this Commission has included the open flow of wells transferred to Texoma amounting to approximately 270,000,000 feet per day; that all of these matters are necessary to be taken into consideration in determining proper re-

serves and were not considered by this Commission as known by it; that the reserves of the Cities Service Gas Company are not in excess of proper reserves as recognized by the gas industry and as owned and held by other major pipe line companies; that none of the gas acreage now held by Cities Service Gas Company was bought or is being held for speculation.

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[fol. 279] EXHIBIT "G" TO BILL OF COMPLAINT

Opinion on rehearing omitted here, being identical with Exhibit "K" on page 74 of this record, except as to signatures and dissent of Chairman Greenleaf which were not included in Exhibit "G."

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EXHIBIT "H" TO BILL OF COMPLAINT

Order dated August 31, 1932, omitted here, being identical with Exhibit "L" on page 84 of this record.

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EXHIBIT "I" TO BILL OF COMPLAINT

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

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EXHIBIT "J" TO BILL OF COMPLAINT

Application for rehearing on opinion and orders omitted here, being identical with Exhibit "N" on behalf of The Wichita Gas Company on page 91 of this record.

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EXHIBIT "K" TO BILL OF COMPLAINT

Supplemental application for rehearing on opinion and orders omitted here, being identical with Exhibit "O" on behalf of The Wichita Gas Company, on page 97 of this record.

EXHIBIT "L" TO BILL OF COMPLAINT

Order for investigation omitted here, being identical with Exhibit "A" on page 38 of this record.

[File endorsement omitted.]

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[fol. 280] IN UNITED STATES DISTRICT COURT

NOTICE OF HEARING IN CASE NO. 1637-N

To the above-named plaintiff and its attorneys of record:

You and each of you are hereby notified that the Defendants in the above entitled cause will on Saturday, September 24, 1932, at 10 o'clock, A. M., or as soon thereafter as the same may be heard, call up for hearing before a three-judge court, to be assembled by the Honorable Orie L. Phillips in the court room of the Federal Building at Topeka, Kansas, their motion to dismiss the bill of complaint filed by you in the above entitled cause, a copy of which motion is attached hereto.

The Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and C. W. Campbell, the Persons Constituting said Commission, Defendants. Chas. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher, Attorneys for Defendants.

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[fol. 281] IN UNITED STATES DISTRICT COURT

[Title omitted]

MOTION TO DISMISS BILL OF COMPLAINT—Filed Sept. 23, 1932

Come now the undersigned defendants and say:

That said Bill of Complaint ought to be dismissed because it appears upon the face of the bill of complaint:

1. That the bill of complaint does not make out or state such a cause of action as to entitle the plaintiff to the relief prayed for or to any relief.

2. That this court is without jurisdiction to try the cause.

Wherefore Defendants pray that the bill of complaint be dismissed and the costs be taxed to the plaintiff.

The Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill, and C. W. Campbell, the Persons Constituting the said Commission, Defendants. , Attorneys for Defendants.

[File endorsement omitted.]

[fol. 282] In United States District Court for the District of Kansas, First Division

In Equity. No. 1637-N

The Wichita Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, and Jesse W. Greenleaf, Thurman Hill, and C. W. Campbell, as Members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, Defendants

In Equity. No. 1638-N

The Hutchinson Gas Company, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1639 N

The Newton Gas Company, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1641-N

The Capital Gas & Electric Company, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1642 N

THE WYANDOTTE COUNTY GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1640 N

THE PITTSBURG GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1643 N

THE CHANUTE GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1644 N

UNION PUBLIC SERVICE COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1645 N

WESTERN DISTRIBUTING COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

[fol. 283] ORDER CONSOLIDATING CAUSES NOS. 1637-N TO 1645-N, INC. Filed Sept. 24, 1932

The above entitled causes came on to be heard on this 24th day of September, 1932, before Honorable Orie L. Phillips, Circuit Judge, Honorable George T. McDermott, Circuit Judge, and Honorable Richard J. Hopkins, District Judge; plaintiff in each case appearing by Robert D. Garver and Robert Stone, its counsel, and the defendants The Pub-

lic Service Commission of the State of Kansas, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, appearing by Earl H. Hatcher, their counsel; and Roland Boynton, Attorney General, appearing by Walter T. Griffin and Everett E. Steerman, his counsel.

It appearing to the court and counsel consenting thereto that the aforesaid cases should be consolidated,

It is hereby ordered, adjudged and decreed that said causes be and they are hereby consolidated for the hearing and for the trial of said causes, and proceedings hereafter may be had and entitled The Wichita Gas Company vs. The Public Service Commission of the State of Kansas et al., being cause No. 1637-N, Consolidated.

It is further ordered, adjudged and decreed that the motion filed by the Attorney General to dismiss as to him is hereby overruled, to which ruling the defendant in open court objected and excepted, which objections and exceptions were made and allowed.

It is further ordered that the motion of the defendants, The Public Service Commission of the State of Kansas, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, constituting said Commission, to dismiss the bill of complaint be and the same is hereby overruled, to which ruling said defendants in open court objected and excepted and exceptions were duly allowed.

Thereupon the court allowed the defendants and each of them seven (7) days in which to file answers to said causes, [fol. 284] counsel in open court accepting such limitation and consenting to the fixing of that date.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, District Judge.

[File endorsement omitted.]

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[fol. 285] IN UNITED STATES DISTRICT COURT

ORDER CONSOLIDATING CASE NO. 1646-N WITH CASE NO. 1637-N —Filed Sept. 24, 1932

Now on this 24th day of September, 1932, it is ordered by the Court that the above entitled case be and the same is

hereby consolidated for the hearing and for the trial thereof with the case entitled The Wichita Gas Company vs. The Public Service Commission of the State of Kansas, et al., being cause No. 1637-N, consolidated.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, District Judge.

[File endorsement omitted.]

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[fol. 286] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF DEFENDANTS IN CASE NO. 1637 N FILED OCT. 3, 1932

The joint and several Answer of the Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and C. W. Campbell, to the bill of complaint of The Wichita Gas Company, a corporation, plaintiff.

These defendants, now and at all times hereafter saving and reserving to themselves, and each of them, all benefit and advantages of exception, which can or may be had or [fol. 287] taken to the many errors, uncertainties and imperfections in the said plaintiff's bill of complaint contained, for answer thereunto or unto so much and such parts thereof as the defendants are advised is or are material or necessary for them to make answer unto, they, these defendants severally answering, say:

1, 2, 3, 4, and 5

They admit the allegations of paragraphs one, two, three, four and five of the bill of complaint.

6

Said defendants say that they have no such information as will enable them to affirm or deny the allegations in paragraph six that plaintiff has no supply of gas for sale and distribution to its customers other than the supply it purchases from the Cities Service Gas Company at the agreed price of forty (40) cents per thousand cubic feet for domes-

tic gas to plaintiff for a less price and plaintiff has no other source of supply available to it and without its present supply cannot carry on its said business.

These defendants answering further say that while it is true that plaintiff, as a legal entity does not produce or manufacture gas for sale or distribution to its customers, it does, by, thru and in conjunction with its affiliated company, the Cities Service Gas Company, both the plaintiff and the Cities Service Gas Company being subsidiaries [fol. 288] of the Cities Service Company, have control thru its holding company, The Cities Service Company, of a natural gas supply.

7

These defendants deny that the present value of plaintiff's property used and useful in rendering the service in which it is engaged is not less than a sum of $2,872,854.00; and further answering these defendants aver that the value of plaintiff's property devoted to the public purpose in supplying its customers with natural gas is substantially less than the valuation claimed by the plaintiff, and defendants further say that with reasonable and necessary operating expenses paid from the gross revenue of plaintiff's gas distributing plant and with lawful rates complained of in effect the property of plaintiff would net to it a reasonable return upon the fair value of its property.

8

Defendants admit the allegations of paragraph eight, except that they deny that under existing rates the present earnings are inadequate and unreasonable.

9, 10, 11, 12, 13, 14, and 15

Defendants admit the allegations of paragraphs nine, ten, eleven, twelve, thirteen, fourteen and fifteen of plaintiff's bill of complaint, except that the defendants deny that the Commission at any time undertook to order plaintiff to make no payments to the Cities Service Gas Company in excess of 29½ cents per M c. f. as alleged in paragraph twelve.

[fol. 289] Defendants admit that on rehearing on August 15, 1932, plaintiff attempted to introduce other evidence in

connection with other matters assigned and alleged as grounds for rehearing in its application set out in plaintiff's bill of complaint as Exhibit "E," but defendants deny that plaintiff was wrongfully and unlawfully denied the right so to do. Defendants further answering allege that the Commission rightfully restricted the rehearing to the allegations of paragraph thirty-nine of plaintiff's said application, the application being granted as to paragraph thirty-nine only, said proceedings were not open for all purposes of the original hearing.

17

Defendants have no information sufficient to enable them to affirm or deny the allegations of paragraph seventeen of the bill of complaint as to what evidence could be introduced concerning matters other than those alleged in paragraph thirty-nine of plaintiff's said application set out in its bill of complaint as Exhibit "E"; defendants answering further allege that the Commission properly restricted the introduction of evidence to paragraph thirty-nine of plaintiff's application for a rehearing set out in plaintiff's bill of complaint as Exhibit "E."

[fol. 290] 18

Defendants admit the allegations of fact made in paragraph eighteen of plaintiff's bill of complaint, and answering further allege that the year ending June 30, 1932, covered but one of the three test periods used by the Commission, and was not alone a proper measure of the reasonableness of the contract between plaintiff and the Cities Service Gas Company.

19

Defendants deny that in the opinion on rehearing, set out in plaintiff's Exhibit "K," that the Commission found that the Cities Service Gas Company was earning only 8.0438 on the value found by the Commission, and deny that the Commission ignored the fact it had no jurisdiction of the Cities Service Gas Company to fix its rate to be charged in interstate commerce and denies it ignored the fact that it had under consideration only the reasonableness of the contract between the Cities Service Gas Company and the plaintiff

as of the time of said investigation and defendants further deny that the Commission unlawfully and arbitrarily proceeded to find the average value of the Cities Service Gas Company over a three year period and the average depreciation and depletion requirements for the same period. The defendants answering further allege that the Commission properly took the test period covering three years in which to determine the reasonableness of the contract and fixed a price to be charged by the Cities Service Gas Company for gas at thirty (30) cents which would produce a return of approximately 7 per cent on the average value of the Cities Service Gas Company's property.

[fol. 291] Defendants answering further allege that due to the affiliation between the plaintiff and the Cities Service Gas Company, the common stock of both companies being owned indirectly by the Cities Service Company that the reasonableness of the contract was properly measured by a return of approximately 7 per cent to the Cities Service Gas Company on the fair value of its property.

20, 21, 22, and 23

Defendants admit the allegations in paragraphs twenty, twenty-one, twenty-two and twenty-three of plaintiff's bill of complaint.

24

Defendants deny the allegations of paragraph twenty-four of plaintiff's bill of complaint that the order issued by the Commission on August 31, 1932, and set out in plaintiff's bill of complaint as Exhibit "L," in which said Commission finds unreasonable and refuses to recognize the plaintiff's contract to the Cities Service Gas Company for the purchase of its supply of gas at the city gate, its contract with Henry L. Doherty & Company, under which plaintiff pays 1¾ per cent of its gross revenues for services rendered to it by said Henry L. Doherty & Company is unnlawful, unreasonable and void because it is in direct violation of the constitution and laws of the State of Kansas and the constitution of the United States, and defendants answering further allege that said order is lawful and reasonable and [fol. 292] not in violation of the laws of Kansas or the United States. Defendants admit that the order issued by the Commission on August 31, 1932, and set out in plain-

tiff's bill of complaint as Exhibit "M," is unlawful and therefore void under the laws of the State of Kansas.

25

Defendants deny that the orders of the Commission, and each and all of them, in so far as they purport to disapprove the contract entered into between plaintiff and the Cities Service Gas Company under the terms of which plaintiff pays to said Cities Service Gas Company the price of 40 cents per M. c. f. for gas sold and delivered to it at the city gate for domestic purposes and in so far as they and each of them purport to disallow as an item of plaintiff's operating expense any sum paid for purchased gas in excess of 30 cents per M. c. f., are unlawful, unreasonable, arbitrary and void for the reasons set out in plaintiff's bill of complaint as follows:—

(a) For the reason that in said opinions, findings and orders said Commission found the value of the property or rate base of the Cities Service Gas Company to be $73,148,510; that the earnings of said company for the year ending June 30, 1932, were $7,963,813 applicable to replacement reserves and return on the fair value of the property; that replacement reserves for said period should be $1,977,591 and that the net income after reserves applicable to return on the value of said property was $5,986,222, which amounts to an earning of only 8.1837 per cent on said Com- [fol. 293] mission's own rate base so found and said Commission's own allowance for replacement reserves, and an earning of only 8.0438 per cent if the sum of $52,297.13 wrongfully and unlawfully disallowed by said Commission as an item of operating expense on account of it being paid to Henry L. Doherty & Company and if the item of $50,000 wrongfully and unlawfully disallowed by said Commission as an item of operating expense for the reason that it represented expenses incurred in said proceedings before said Commission be included in expenses. And plaintiff alleges that said earning is less than a reasonable rate of return for said Cities Service Gas Company considering the unusual hazards of its business and is less than a return necessary to attract capital to said business at this time and under present conditions, it therefore being apparent on the face of said opinions, findings and orders that the contract between plaintiff and the Cities Service Gas Company.

is reasonable, does not indicate any absence of arm's length dealing between plaintiff and said company on account of their affiliation and should not have been disapproved.

(b) For the reason that the attempt of said Commission in said opinions, findings and orders, and each of them, to avoid the clear and undisputed reasonableness of the earnings of the said Cities Service Gas Company by averaging the earnings over a period of years and applying same to an average value of property, is unreasonable, unjust and unlawful and does not change or alter the Commission's [fol. 294] findings that said Cities Service Gas Company earned only 8.1837 per cent on the value of its property found by said Commission after deducting reserves approved by said Commission, said Commission having no jurisdiction, power or authority to determine the present reasonableness or unreasonableness of said contract on the property values and earnings of said Cities Service Gas Company as of any time other than the time said opinions, findings and orders were entered.

(c) For the reason that said opinions, findings and orders on their face show the contract between plaintiff and the Cities Service Gas Company to be such a contract as would have been entered into by parties unaffiliated dealing at arm's length and in the general and open market subject to the usual safeguards of bargaining and competition.

(d) For the reason that said Commission in dealing with the item of interest during construction, as appears in Exhibit "C," pages 78 and 79, found that 6 per cent was a proper rate to use for this item notwithstanding the fact that it is common knowledge of which the Court may take judicial notice that money could not be procured at the time of said hearing at such rate and notwithstanding the fact that the Commission found 7 per cent to be a proper rate of return for the Cities Service Gas Company after the completion of its plant and after the same was placed in operation, said Commission by adopting said 6 per cent having thereby eliminated from the rate base of the Cities Service Gas Company approximately one million dollars.

(e) For the reason that in its consideration of the item of going value as appears in Exhibit "C," pages 85 to 88,

the Commission unlawfully, unreasonably, arbitrarily and capriciously allowed only the sum of $4,000,000 on its own valuation of $73,148,510 and ignored all the evidence in the case on the subject, such evidence consisting of the testimony of F. C. Hamilton, engineer for plaintiff, that a [fol. 296] proper allowance would be $8,808,582, and the testimony of its own witness, E. B. Black, that such value was $3,820,00 , and ignored the uniform practice of courts and commissions to allow for such item approximately 10 per cent of the rate base, by which arbitrary and unreasonable action said Commission reduced the proper rate base of said Cities Service Gas Company over six million dollars.

(f) For the reason that said Commission in its consideration of the item of gas leases and reserves of said Cities Service Gas Company after finding that the present fair market value of such reserves was $6,279,237 and the present book value $6,573,489.70, as appears in Exhibit "C" at pages 99 and 100, unreasonably and arbitrarily found that most of said reserves were not used and useful and allowed for said item only the sum of $2,874,990, thereby eliminating from the rate base of the Cities Service Gas Company the sum of $3,404,847, which on its own finding of present market value should have been included; and said Commission on rehearing wrongfully refused to permit plaintiff to show that the reserves allowed by said Commission were inadequate and would result in absolute failure of service as is shown by Exhibit "G" hereto attached. By all of which unreasonable, arbitrary and unwarranted conduct said Commission undertook, without one word of evidence from any witness in support of its finding as to what would constitute proper reserves for said Cities Service Gas Company, to substitute its own judgment and to usurp the duties of the officers of said company upon whom the responsibility for service rests.

(g) For the reason that said Commission eliminated from the replacement reserves of the Cities Service Gas Company all lease rentals and development expense on leases which it wrongfully found to be not used and useful, amounting to the sum of $532,530.77, as appears from said order, Exhibit "C," at page 112, and also eliminated the [fol. 296] reserve which must be accrued for amortizing the cost of said leases amounting to $514,981.68, as appears

from said order, Exhibit "C," page 112, or a total of $847,512.45.

(h) For the reason that said Commission in determining the rate base of the Cities Service Gas Company depreciated overheads, thereby eliminating from said rate base the sum of $1,014,392 without making any allowance in replacement reserves to compensate for such depreciation, which reserve should have been included in the amount of $30,443 annually, as appears by the opinion of said Commission, Exhibit "C," page 111, or said overheads should not have been depreciated and said rate base should have been accordingly increased.

(i) For the reason that it is apparent on the face of said opinions, findings and orders that if said Commission had made proper allowances in the rate base of the Cities Service Gas Company for interest during construction, going value and leases and gas reserves, and had made a reasonable allowance for replacement reserves, the rate base of said Cities Service Gas Company would be so increased and its earnings after replacement reserves so decreased on the Commission's own findings that the present earnings of said company after reserves and applicable for return would amount to less than 6½ per cent on such rate base.

(j) For the reason that said Cities Service Gas Company is engaged in inter-state commerce the right to control which is vested by the Constitution of the United States exclusively in Congress, and said Commission is without [fol. 297] jurisdiction to fix a rate for said Company or to proceed in the manner attempted in said proceedings so instituted by it or to make the orders herein set out.

(k) For the reason that the value of the property of the Cities Service Gas Company used and useful in carrying on its said business on August 31st, 1932, and at all times since that date, was and is not less than $105,857,402, and the finding by said Commission in said opinion and orders of August 31st, 1932, that said value was only the sum of $73,148,510 is unreasonable, unjust and contrary to all the evidence introduced before said Commission.

(l) For the reason that if the price of 30 cents for gas sold for domestic purposes at the city gate by the Cities Service Gas Company had been in effect during the year

ending June 30, 1932, and if said rate of 30 cents per M. c. f. is applied to the actual business transacted by said Cities Service Gas Company for said period, its gross earnings would have been reduced in the sum of $1,926,145.07 and its net earnings before replacement reserves would have been $5,935,371.78, which is a return of only 5.4 per cent on said Commission's own rate base as found in said opinion and orders of $73,148,510, which rate base is entirely unreasonable, unjust and inadequate as hereinbefore alleged after deducting the Commission's own unreasonable, unjust and inadequate allowance for replacement reserves, and if said rate had been so applied during said period the earnings of the Cities Service Gas Company would have amounted to only 5.6 per cent on the present fair value of its property of $105,857,402 for all the purposes of replacement reserves, depreciation, amortization, depletion and return.

[fol. 298] (m) For the reason that in its consideration of the reasonableness of said contract between plaintiff and Cities Service Gas Company for plaintiff's supply of gas at the city gate it was the duty of said Commission, in the absence of any jurisdiction, power or authority over the interstate business of said company to consider its operations, business and experience as the same actually existed and were being carried on by said company, without undertaking or attempting to determine the reasonableness or usefulness of its gas reserves or any other item of its property and without undertaking or attempting to determine the reasonableness of its operating expenses, or any item thereof, the jurisdiction of said Commission being limited to the determination of the reasonableness of such contract under existing operating conditions of the Cities Service Gas Company and said Commission being without jurisdiction, power or authority to regulate said company as attempted in said opinions, findings and orders.

(n) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(o) For the reason that the finding of said Commission that the contract between plaintiff and Cities Service Gas Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceedings and is entirely without support in the evidence.

[fol. 299] (p) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A", herein and all subsequent proceedings of said Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to ascertain the reasonableness of a rate or charge to be made by a public utility.

Defendants answering further allege that the orders of said Commission in so far as they purport to disapprove the contract entered into between plaintiff and The Cities Service Gas Company and in so far as they disallow items of plaintiff's operating expense, any sum for purchase of gas in excess of 30 cents per M. c. f. are reasonable and valid.

26

Defendants deny the allegations in paragraph twenty six in plaintiff's bill of complaint in which plaintiff further alleges that said opinion and orders of said Commission entered August 31st, 1932, and each and all of them, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which plaintiff pays to said Henry L. Doherty & Company $1\frac{3}{4}$ per cent of its gross revenues, are unreasonable, unjust and unlawful and void for the following reasons:

[fol. 300] (a) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(b) For the reason that said Commission in said investigation so held by it did not have before it any evidence whatever as to the value of plaintiff's property used and useful in rendering the service in which it is engaged, its operating experience or the reasonableness of its existing rates, and unlawfully, unreasonably and unjustly refused to permit plaintiff to introduce any such evidence and was therefore not in a position to determine whether or not the disallowance of said item of operating expense would affect the rates then being charged by plaintiff or warrant a decrease in rates to consumers.

(c) For the reason that said Commission was without jurisdiction, power or authority to disallow said item of plaintiff's operating expense in the absence of an express finding that existing rates were unreasonable by reason of the inclusion of said item in plaintiff's operating expenses and the substitution of a new rate in lieu of the old rate so found to be unreasonable.

(d) For the reason that plaintiff offered to show to said Commission in said original proceeding and on rehearing, as shown by Exhibit "F" hereto attached, that under existing rates it was earning only 7.2 per cent on the present fair value of its property, and the disallowance of said item in plaintiff's operating expenses could not possibly affect the reasonableness of its existing rates or give jurisdiction to the Commission to reduce the same on account of the disallowance of said item.

[fol. 301] (e) For the reason that said Commission by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment has unlawfully and unreasonably undertaken the management of plaintiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

(f) For the reason that the finding of said Commission that the contract between plaintiff and Henry L. Doherty & Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such

payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceeding and is entirely without support in the evidence, while in truth and fact services of great value were and are being rendered by said Henry L. Doherty & Company, to wit: the amount charged.

Defendants answering further allege that the opinion and orders of the Commission entered August 31, 1932, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which the plaintiff pays to Henry L. Doherty & Company $1\frac{3}{4}$ per cent of its gross revenues, are reasonable and valid, and is a proper exercise of the jurisdiction, power and authority of the Public Service Commission for the State of Kansas.

27

Defendants deny all of the allegations of paragraph twenty-seven of plaintiff's bill of complaint except that [fol. 302] they admit that Exhibit "M" directing plaintiff to reduce its rates to consumers as of September 1, 1932, is in violation of the statutes of the State of Kansas.

28

Defendants deny the allegations of paragraph twenty-eight, set out in plaintiff's bill of complaint, and answering further allege that all the distributing companies joined in the investigation before the Commission were similarly situated and all of their interests were common in the matters under investigation by the Commission, and that plaintiff was lawfully compelled to appear before the Commission for the purpose of investigating the reasonableness of charges made by affiliated or holding companies.

The defendants answering further allege that all of the voting stock except qualifying directors' share, of the Cities Service Gas Company, plaintiff herein, is owned by the Empire Gas & Fuel Company, and that all of the voting stock, except qualifying directors' share, of the Empire Gas & Fuel Company, is owned by the Cities Service Company; that all of the voting stock, except qualifying directors' shares, of the plaintiff company is owned by the Gas Service Company; that all of the voting stock of the Gas Service Company is owned by the Cities Service Company; that

because of this ownership and control of the plaintiff company, and the Cities Service Gas Company by the Cities Service Company, they are subjected to one management and are not able to deal freely at arm's length with each other; that Henry L. Doherty & Company owns for all practical purposes the voting control of the common stock of the Cities Service Company and that under a contract between Henry L. Doherty & Company, plaintiff and the de-
[fol. 303] fendant distributing companies, and all other companies affiliated with the Cities Service Company, Henry L. Doherty & Company is for all practical purposes operator and manager of both the plaintiff and the Cities Service Gas Company, and that the Auditor of Henry L. Doherty & Company, who is appointed by Henry L. Doherty, is given the authority to appoint or remove any officer holding a responsible position in the plaintiff company, or the Cities Service Gas Company.

29

Defendants deny all the allegations set out in paragraph twenty-nine of plaintiff's bill of complaint.

30

Defendants have no information sufficient to enable them to affirm or deny the allegations that plaintiff cannot procure gas for less than 40 cents per M. c. f., but defendants are informed and believe and so aver that said plaintiff has made no reasonable or diligent effort to procure gas for less than 40 cents per M. c. f.

These answering defendants further say that both the plaintiff and the Cities Service Gas Company are thru stock ownership owned and controlled by the Cities Service Company and because of such relationship it is not in position to negotiate with the Cities Service Gas Company as to the price paid for gas, but it must pay and the Cities Service Gas Company must receive the price dictated by the Cities Service Company.

[fol. 304] 31

Defendants deny all of the allegations set out in paragraph thirty-one of the plaintiff's bill of complaint.

32

The defendants have no information sufficient to enable them to affirm or deny the allegations set out in paragraph thirty-two of the bill of complaint in which it is alleged that the State of Texas has placed an absolute and unqualified limit on the takes of wells in the gas reserves of the Cities Service Gas Company in Texas. Defendants answering further allege that if such an order were put into effect it would tend to decrease the value which the Commission placed upon the gas reserves and would not tend to limit the amount of gas which could be taken from such reserves, and that the gas reserves allowed by the Commission as set out in the plaintiff's bill of complaint are entirely adequate, sufficient, and reasonable.

33

Defendants deny that plaintiff is without adequate remedy at law and will suffer irreparable injury unless the injunctive relief prayed for is accorded. These defendants answering further allege that the order issued by the Commission on August 31, 1932, was the reasonable exercise of the jurisdiction conferred upon them by the laws of the State of Kansas, and that the plaintiff has not thereby been denied any of the rights which they may have under the constitution of the State of Kansas or the constitution of the United States.

[fol. 305] Defendants admit that that part of its order, Exhibit "M" to plaintiff's bill of complaint, dated August 31, 1932, wherein the defendant commission ordered the distributing companies from and after September 1, 1932, to deduct the excess between what the distributing companies were then paying for gas at the city gate and thirty cents per M. c. f. of gas and pass the difference to the consumer, is null and void, and further allege that these defendants have abandoned said order and allege that said Commission now has no intention of enforcing or attempting to enforce said order; that the defendant Commission relies upon and alleges it has the right to enforce its order made on August 31, 1932, Exhibit "L" attached to plaintiff's bill of complaint, whereby it ordered said distributing companies to show cause why they and each of them should not pass said reduction in price to be paid for gas at the city gate on to the consumers and in this connection these

defendants allege that such proceedings contemplate that an investigation be made as required by law as to each of said distributing companies to determine whether the earnings of said distributing company based upon the fair value of their property are excessive and unreasonable, after giving effect to the said thirty cent gate rate and all other facts bearing upon the question.

Defendants allege that unless and until said hearing is had and these defendants make an order determining that said rate to the consumers be reduced, that its said order, Exhibit "L," will not and may not affect the plaintiff, and that until an order is made reducing said rate to said distributing companies by the consideration of said reduced gate rate this court has not and will not have jurisdiction of the subject matter of this action.

[fol. 306] Wherefore Defendants, having answered all and singular those parts of the bill of complaint material and necessary to answer, pray that notwithstanding they have answered all the allegations of the bill of complaint that the court dismiss the bill of complaint for the reason and on the ground that it plainly appears from the averments therein contained that no federal question is raised by the bill of complaint and this court is without jurisdiction to try the cause. But these answering defendants reserve and save to themselves all of their rights in the presentation of evidence and request a hearing upon the matters of the issues of fact and law involved in this cause, in the event it should be determined that said bill of complaint be not dismissed for want of jurisdiction appearing therein; and further defendants pray plaintiff take nothing by reason of the allegations in said bill of complaint; that no permanent injunction be granted herein, but that these defendants be hence dismissed with reasonable costs and charges.

Chas. D. Welch, Harry Castor, Chas. W. Steiger,
E. H. Hatcher, Attorneys for Defendants.

[File endorsement omitted.]

[fol. 307] In United States District Court

Answer of Defendants in Case No. 1646 N Filed Oct. 3, 1932

The joint and several Answer of the Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and Charles W. Campbell, to the bill of complaint of the Cities Service Gas Company, a corporation, plaintiff.

These defendants now, and at all times hereafter, saving and reserving to themselves and each of them, all benefit and advantage of exception which can or may be had or taken to the many errors, uncertainties and other imperfections in the said bill of complaint contained, for answer thereunto or unto so much and such parts thereof as these defendants are advised is or are material or necessary for them to make answer unto, them, these defendants severally answering, say:

[fol. 308] I

They admit the allegations of paragraph one of said bill of complaint.

II

Defendants admit the allegations of paragraph two set out on page four of the bill of complaint, and deny all of the allegations of paragraph two set out on page five of the bill of complaint, and further deny and it is not true that the orders issued by the Commission, dated August 31, 1932, and attached to the bill of complaint as Exhibits "A" and "B" are confiscatory of plaintiff's property used and useful, in furnishing service and natural gas to the defendant distributing companies, and denies that the orders therefore are in contravention of any section of the constitution of the United States or any amendment thereto.

Defendants answering further allege that the Cities Service Gas Company, through common stock ownership is owned and controlled by the Cities Service Company, and that all of the distributing plants made defendants herein and against which the orders of the Commission were directed are also through stock ownership owned and controlled by the Cities Service Company, and that because of the affiliation of the plaintiff, the Cities Service Gas Com-

pany and of the defendants, the distributing plants named herein, and the unity of control thus engendered, the interstate carriage of the gas by the Cities Service Gas Company is combined with its local distribution in what is in practical effect one organization; that the opportunity exists for one member of the combination to charge the other an unreasonable rate for the gas furnished, and this is in fact done, and the unreasonable charge is made in part the basis of the retail rate.

[fol. 309] III

Defendants admit the allegations of paragraph three of the bill of complaint except that defendant alleges that only about 42,000 acres of the 1,225,000 acres of the gas leases owned by plaintiff, are drilled and producing gas and that approximately 1,000,000 acres of said gas leases are not available to plaintiff's pipe lines, that most of said 1,000,000 acres are what is known as "Wild Cat" leases and that the remainder of its leases outside those situated in the sweet proven area in the Amarillo field are located in the Hugoton field in Kansas and Oklahoma, and that said leases in the Hugoton field consisting of approximately 123,440 acres, although valuable for gas, are distant from the plaintiff's pipe line a distance of ninety miles, and except that defendant denies that all of said 1,225,000 acres of gas leases were acquired for the purpose of insuring a dependable supply of gas for its customers, and defendant alleges that all of the gas leases of plaintiff in excess of 71,276 acres were acquired and are held for speculative purposes.

Answering further defendants allege that in all cases where the plaintiffs, by means of its said pipe line system delivered gas in wholesale quantities to other purchasers not affiliated with the plaintiff's, that the plaintiff is selling its gas at much less than 40 cents per M. c. f., or has [fol. 310] a monopoly on the pipe line business, so that the independent companies are unable to otherwise obtain gas, and must pay to the plaintiff such unreasonable charge as it may exact.

IV

Defendants admit the first two sub-paragraphs of paragraph four of the bill of complaint, but deny the last subparagraph, and further deny that the rates or prices at

which plaintiff has been or is now supplying the defendant distributing companies with natural gas are reasonable and lawful, and further deny that the agreements were entered into after negotiations allowing for the protection of the defendant distributing companies. Defendants admit the allegations contained in paragraph four in so far as it sets out the price which the defendant is charging each of the defendant distributing companies for pipe line gas. The defendants answering further, allege that the agreement under which the plaintiff sells pipe line gas to the defendant distributing companies is a day to day agreement and does not bind the defendants for any length of time.

V

Defendants admit the allegations of the first four and last sub-paragraphs of paragraph five of the bill of complaint but denies the allegations of the fifth sub-paragraph of paragraph five, and further deny that the evidence and [fol. 311] exhibits introduced, and the investigation before the Commission disclosed that the contracts between the plaintiff and defendant distributing companies were reasonable, and such contract as would be entered into by persons dealing at arm's length; that the fair value of the property of plaintiff on September 1, 1931, used or useful, in the business of supplying natural gas to the defendant distributing companies, was $105,857,402.00, and alleges that the value of the plaintiff's property used or useful in the business of supplying natural gas to the defendant distributing companies is and was materially less than this amount, and that its net earnings from operations after depreciation was greatly in excess of a reasonable return. The defendants further deny that the rate of return which each of the defendant distributing companies was making at the time of the investigation was inadequate, unreasonable or confiscatory.

VI

Defendants admit the allegations of paragraph six of the bill of complaint.

VII

Defendants admit the allegations of paragraph seven of the bill of complaint.

VIII

Defendants admit the allegations of first four sub-paragraphs of paragraph eight of the bill of complaint. Defendants have no information sufficient to enable them to [fol. 312] affirm or deny the allegations set out in sub-paragraphs five and six of paragraph eight of the bill of complaint as to what showing the defendant distributing companies could have made under such allegations as to the plaintiff's gas reserve. The defendants deny that the Public Service Commission wrongfully denied to each of the defendant distributing companies the right to make proof on the rehearing of the offer set out in the bill of complaint as Exhibit "A", but that the Commission rightfully permitted only the proof of the earnings, expenses and net income of the plaintiff for the year ending June 30, 1932, as this was the only new matter presented in the application for rehearing.

IX

The Defendants admit the allegations of fact made in paragraph nine of plaintiff's bill of complaint. [fol. 313] Defendants deny that at no time has the defendant held itself out as public utility or common carrier of gas, and has at no time engaged in the business of common carrier, and denies that the entire properties of plaintiff have been devoted chiefly to a private enterprise. Answering further defendants allege that plaintiff is holding itself out as a public utility and common carrier of gas. Defendants admit that part of plaintiff's gas moves in interstate commerce, but denies, and it is not true that all of such gas so moves. Defendants deny the allegation that the pipe line company did not submit itself to the jurisdiction of the Commission, and allege that the officers and employes of the plaintiff pipe line company appeared before the Commission and presented the case for the plaintiff pipe line company, and has assumed the cost of the investigation, and has already set up such cost for amortization purposes as an expense of the plaintiff pipe line company.

The Defendants admit that the contracts for gas made by the plaintiff to the defendant distributing companies were in existence prior to the investigation by the Public

Service Commission, but deny that such charges and rates are fair and reasonable.

[fol. 314] The defendants deny all of the allegations of paragraph eleven of the bill of complaint, and answering further allege that the Public Service Commission properly found the value of plaintiff's property used or useful in its business was only $73,148,510, and that the plaintiff's net depreciation allowance should be $1,977,591, and that the Commission's findings that 30 cents per M. c. f. was a proper charge for the plaintiff to make to the defendant distributing companies, was reasonable and proper and within the jurisdiction of the Commission, due to the affiliated relationship between the plaintiff and the defendant distributing companies, and the orders were not in interference with inter-state commerce; nor impairment of the operation of contractual rights, nor in contravention to the constitution of the United States as amended.

## XII

The Defendants deny the allegations of paragraph twelve of the bill of complaint, and further deny that 30 cents per M. c. f. for gas furnished will not afford the plaintiff a fair return upon the fair value of its property used and useful in its business, and deny that such return will be confisca-
[fol. 315] tory, or that plaintiff's property will be taken without due process of law, or the obligations of contract will be interfered with. The defendants answering further allege that the order of the Public Service Commission set out as Exhibits "H" and "I", in plaintiff's bill of complaint, are not addressed to the plaintiff, and do not in any way interfere with its property or contract right, and that it shows upon the face of the bill of complaint that the rights of the plaintiff are in no way interfered with.

## XIII

Defendants deny all of the allegations of paragraph thirteen of the bill of complaint, and further deny the allegation that for the plaintiff to sell and deliver gas to the defendant distributing companies at the price fixed by the Public Service Commission in its orders would produce a fair and reasonable return on the value of its property used or useful in its business, and deny that the order would

result in the destruction of the plaintiff's property and business.

XIV

Defendants admit the allegations of fact in paragraph fourteen of the bill of complaint in so far as it alleges the [fol. 316] ownership of stock and corporate relationship of the Empire Gas and Fuel Company, and Cities Service Gas Company, the Cities Service Company, the Gas Service Company, and the defendant distributing companies, but denies that the plaintiff and defendant distributing companies are affiliated companies only because of technical provisions of Chapter 259 of the Session laws of the State of Kansas for 1931, and that the business of the plaintiff and the defendant distributing companies is carried on in an independent manner as if such affiliation did not exist, and denies that the common owner of both the plaintiff and defendant distributing companies would not be benefited from profits of the plaintiff, Cities Service Gas Company. The defendants answering further allege that all of the voting stock, except qualifying director's share, of the Cities Service Gas Company, plaintiff herein, is owned by the Empire Gas and Fuel Company, and that all of the voting stock except qualifying directors' share, of the empire Gas and Fuel Company, is owned by the Cities Service Company; that all of the voting stock, except qualifying directors' shares, of the defendant distributing companies, is owned by the Gas Service Company, and that all of the voting stock of the Gas Service Company is owned by the Cities Service Company; that because of this ownership and control of the plaintiff company, and the defendant distributing companies by the Cities Service Company, they are subjected to one management and are not able to deal freely at arm's length with each other; that Henry L. Doherty & Company owns for all practicable purposes the [fol. 317] voting control of the common stock of the Cities Service Company, and that under a contract between Henry L. Doherty & Company, plaintiff and the defendant distributing companies, and all other companies affiliated with the Cities Service Company, Henry L. Doherty & Company is for all practical purposes operator and manager of both the plaintiff and defendant distributing companies, and that the Auditor of Henry L. Doherty & Company who is

appointed by Henry L. Doherty, is given the authority to appoint or remove an officer holding a responsible position in the plaintiff company, or the defendant distributing companies.

XV

Defendants deny all of the allegations of paragraph fifteen of the plaintiff's bill of complaint, and further deny that the Public Service Commission arbitrarily and capriciously substituted its judgment for the judgment of the officers and directors of the plaintiff in finding the amount of gas reserve necessary to adequately supply plaintiff's customers, and wrongfully excluded from the valuation of plaintiff's property all other gas lines owned by it. The defendants answering further allege that the Public Service Commission included in the valuation of plaintiff's property [fol. 318] gas reserves in an amount sufficient to last it over a period of twenty years, and that such allowance was liberal to the extent of unreasonableness, and was a greater allowance than the present customers of the plaintiff company should be required to carry. Defendants further allege that a great number of the gas reserves that the respondents contended should be placed in the valuation of the plaintiff's property are of doubtful value for gas and were from fifty to ninety miles from the plaintiff's pipe line, and could not be used, and is not used and useful in the plaintiff's business of supplying natural gas to the defendant distributing companies, and that the same were acquired and held for speculative purposes.

XVI

The defendants admit all of the allegations of fact in paragraph sixteen of the plaintiff's bill of complaint, except the allegations and conclusions pertaining to the Public Utility laws of the State of Kansas, and to the statements relating thereto set out in the last part of said paragraph.

[fol. 319]

XVII

Defendants admit all of the allegations of fact contained in paragraph seventeen of the bill of complaint, except the last sentence, which defendants deny, and further deny that the price which the plaintiff company charges the defendant distributing companies for gas is a fair and reason-

able price, and answering further the defendants allege that the price charged by the plaintiff to the defendant distributing companies for gas is unfair and unreasonable and is in excess of the amount necessary for the plaintiff to receive in order to maintain its said pipe line system and business and produce a reasonable profit therefrom.

XVIII

Defendants deny all the allegations in paragraph eighteen of plaintiff's bill of complaint and defendants answering further allege that Henry L. Doherty & Company has in addition to the 1¾ per cent of the annual gross income from sale of natural gas to persons and companies other than the distributing companies, defendants herein, and other affiliated companies, charged the plaintiff company specifically for all services rendered and that the 1¾ per cent payment has gone into the treasury of the Cities Service Company to take care of its operating expenses and the cost of selling its securities and the plaintiff and the defendant distributing companies have derived no benefit [fol. 320] therefrom; answering further paragraph eighteen of plaintiff's bill of complaint, defendants allege that a reduction of ten per cent in the price of gas sold to the defendant distributing companies by the plaintiff would net the plaintiff company a reasonable return upon the value of its property used and useful in serving its customers.

XIX

Defendants deny all the allegations in paragraph nineteen of plaintiff's bill of complaint; answering further defendants allege that the Commission proceeded under the investigation of the reasonableness of charges made by holding or affiliated companies to the defendant distributing companies in an orderly manner and under the jurisdiction vested in them by the statutes of Kansas, and after a careful investigation in which it considered all of the evidence it found that 30 cents per M. c. f. was a reasonable price for the plaintiff to charge to the affiliated distributing companies for gas, and issued an order in accordance therewith, being Exhibit "H" of plaintiff's bill of complaint, and in conformity with the laws of the State of Kansas regu-

lating the practices and acts of public utilities, and such order is reasonable and lawful.

[fol. 321] XX

Defendants deny all the allegations of paragraph twenty in plaintiff's bill of complaint, and answering further allege that the Commission took into consideration the plaintiff's system as a whole in arriving at the value of its property used and useful in serving its consumers and arrived at a uniform rate for the system as a whole in conformity with the evidence submitted in the investigation and the allegations of respondents that the plaintiff system was not possible of segregation into zones for the purpose of fixing rates and by this process the Commission considered all the property of the plaintiff and made a liberal allowance for gas reserves for the future use of plaintiff in serving its customers, and the proceedings and findings of the Commission are reasonable and should be permitted to stand.

XXI

The defendants deny all the allegations of paragraph twenty one in plaintiff's bill of complaint and allege further that the order of the Commission finding .30 cents per M. c. f. to be a reasonable price for gas sold by the plaintiff to the defendant distributing companies is reasonable and will cause no loss in the assets and properties of the plaintiff company.

[fol. 322] XXII

Defendants admit that each and all the distributing company defendants are interested in the subject matter of this controversy and allege further that each and all distributing company defendants have filed separate and several complaints in the subject matter of this controversy, but defendants deny that the distributing company defendants will be compelled to breach their respective gas purchase contracts with the plaintiff if the orders of the Commission are permitted to stand, and further allege that if a reasonable price is charged by the plaintiff herein to the distributing company defendants for gas as found by the Commission, and under the law required, the contract rights of the plaintiff will not be affected.

## XXIII

The defendants deny that the orders complained of herein violate any of the plaintiff's rights under the federal constitution and deny that the orders in any way interfere with inter state commerce.

## XXIV

Defendants deny all the allegations of paragraph twenty four of the bill of complaint.

[fol. 323] XXV

Defendants deny all the allegations of paragraph twenty five of the bill of complaint and allege that if the plaintiff will charge a reasonable price for gas sold to the distributing company defendants as found by the Commission and required by law, its business will not be interfered with

## XXVI

Defendants further answering deny that the plaintiff has no plain, speedy or adequate remedy at law. Defendants admit that that part of its order, Exhibit "I" to plaintiff's bill of complaint, dated August 31, 1932, wherein the defendant commission ordered the distributing companies from and after September 1, 1932, to deduct the excess between what the distributing companies were then paying for gas at the city gate and thirty cents per M. c. f. of gas and pass the difference to the consumer, is null and void, and further allege that these defendants have abandoned said order and allege that said Commission now has no intention of enforcing or attempting to enforce said order; that the defendant Commission relies upon and alleges it has the [fol. 324] right to enforce its order made on August 31, 1932, Exhibit "H" attached to plaintiff's bill of complaint, whereby it ordered said distributing companies to show cause why they and each of them should not pass said reduction in price to be paid for gas at the city gate on to the consumers and in this connection these defendants allege that such proceedings contemplate that an investigation be made as required by law as to each of said distributing companies to determine whether the earnings of said distributing company based upon the fair value of their property are excessive and unreasonable, after giving effect to the said

thirty cent gate rate and all other facts bearing upon the question.

Defendants allege that unless and until said hearing is had and these defendants make an order determining that said rate to the consumers be reduced, that its said order, Exhibit "H", will not and may not affect the plaintiff, and that until an order is made reducing said rate to said distributing companies by the consideration of said reduced gate rate this court has not and will not have jurisdiction of the subject matter of this action.

Wherefore Defendants have answered all and singular those parts of the bill of complaint material and necessary to answer, pray that notwithstanding they have answered all the allegations of the bill of complaint that the [fol. 325] court dismiss the bill of complaint *that the court dismiss the bill of complaint* for the reason and on the ground that it plainly appears in the averments therein contained that the plaintiff has failed to state a cause of action over which this court has jurisdiction. But these answering defendants save and reserve to themselves all their rights in the presentation of evidence and request a hearing upon the matters of the issues of fact and law involved in this cause in the event it should be determined that said bill of complaint be not dismissed for the want of jurisdiction of this court; and further defendants pray that plaintiff take nothing by reason of the allegations in this said bill of complaint; that no permanent injunction be granted herein, but that these defendants be hence dismissed with reasonable costs and charges.

Chas. D. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher.

[File endorsement omitted.]

[Fol. 320] In United States District Court for the District of Kansas, First Division

In Equity. No. 1637 N

The Wichita Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas et al., Defendants

In Equity. No. 1638 N

The Hutchinson Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1639 N

The Newton Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1640 N

The Pittsburg Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1641 N

The Capital Gas & Electric Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1642 N

THE WYANDOTTE COUNTY GAS COMPANY, a Corporation, Plaintiff

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1643 N

[fol. 327] THE GIRARD GAS COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1644 N

UNION PUBLIC SERVICE COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1645 N

THE WESTERN DISTRIBUTING COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1646 N

CITIES SERVICE GAS COMPANY, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

Appearances:

For Plaintiffs: James W. Finley, R. E. Cullison, Chas. A. Frueauff, Robt. S. Sloan, Fred Robertson, J. O. Emerson, Robt. D. Garver, Robert Stone.

For Defendants: Chas. D. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher.

Before Phillips and McDermott, Circuit Judges, and Hopkins, District Judge.

OPINION Filed Jan. 5, 1933

PHILLIPS, circuit judge, delivered the opinion of the court:

The Cities Service Gas Company, a Delaware corporation, is engaged in the business of producing and transporting gas from Texas and Oklahoma and delivering it to distributing companies along its line, among which are the [fol. 328] following in the state of Kansas: The Wichita Gas Company, The Hutchinson Gas Company, The Pittsburg Gas Company, The Capital Gas & Electric Company, The Newton Gas Company, The Girard Gas Company, The Wyandotte County Gas Company, The Union Public Service Company, and The Western Distributing Company.

The common stock of each of such distributing companies, except the qualifying directors' shares, is owned by the Gas Service Company, a corporation. The stock of the Gas Service Company, except the qualifying directors' shares is owned by the Cities Service Company, a Delaware corporation. The stock of the Cities Service Gas Company, except the qualifying directors' shares, is owned by the Empire Gas & Fuel Company. The stock of the Empire Gas & Fuel Company, except the qualifying directors' shares, is owned by the Cities Service Company.

The Western Distributing Company is a West Virginia corporation and a citizen of that state. The Union Public Service Company is a Delaware corporation and a citizen of that state. The other distributing companies are Kansas corporations.

The Cities Service Gas Company furnishes gas to the distributing companies at the city gates under day to day contracts, which are oral, at forty cents per thousand cubic feet. Each of the distributing companies has contracted to pay Henry L. Doherty & Company one and three-fourths per cent of the gross revenue, a per diem charge and expenses for certain specific services, and an engineering fee of five per cent of the cost of new construction, in consideration of which Henry L. Doherty & Company main-

tains legal, managerial, engineering, accounting and purchasing staffs whose services are available to the distributing companies.

Each of the distributing companies has also entered into a contract with the Gas Service Company under which the [fol. 329] latter furnishes and the former pays for certain services. This contract has been approved by the Commission and is not in controversy here.

On July 2, 1931, the Public Service Commission commenced a proceeding against the corporations hereinbefore named, except the Cities Service Company and the Cities Service Gas Company. It found that the reasonableness of the contracts hereinbefore referred to, and the charges made for services and commodities furnished thereunder, should be inquired into and a determination made of the amounts which properly should be set up as operating expense of the distributing companies on account of expenditures made for such commodities and services under such contracts, and entered an order on such findings for a hearing to inquire into the reasonableness of such contracts and charges, and directed that respondents in such proceeding furnish such information concerning such contracts as the Commission might desire, and "show cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers."

After a hearing, the Commission on July 20, 1932, made findings to the effect that any amounts paid by the distributing companies under their contracts with Henry L. Doherty & Company were unreasonable, and that any amounts paid by the distributing companies to the Cities Service Gas Company for gas in excess of 29.5 cents per thousand cubic feet at the city gates were unreasonable, and ordered that on and after August 1, 1932, the distributing companies (1) cease setting up on their books as operating expenses the one and three-fourths per cent payments to Henry L. Doherty & Company and any payments for gas to the Cities Service Gas Company in excess of 29.5 cents per thousand cubic feet, (2) give no consideration to any such payments in fixing their rates to domestic [fol. 330] consumers, (3) reduce their rates to their con-

sumers proportionately, pending a final determination of their rates; and show cause on September 1, 1932, why such reductions should not be made permanent.

A petition for rehearing was filed by the respondents setting up fifty one grounds. A rehearing, limited to one of such grounds, was granted. After such rehearing, the Commission increased its finding of a reasonable charge for gas at the city gates from 29.5 to 30 cents, and with that modification and the necessary changes in dates, on August 31, 1932, re-entered its order of July 20 in the form of two orders.

The material portions of the first of such orders is as follows:

"That on and after the first day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three fourths per cent charge, and also any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

"That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10 o'clock a. m., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable."

The material portions of the second of such orders is as follows:

"It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

"All distributing companies paying a gate rate in excess of 30 cents per M. C. F., shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer."

[fol. 331] The nine distributing companies and the Cities Service Gas Company brought separate suits in equity to enjoin the enforcement of the two orders of August 31, 1932.

The Newton Gas Company filed a cross bill in each of the suits brought by the distributing companies in which it challenged the right of the Commission to join it with the other utilities in one joint proceeding. Counsel for the Newton Gas Company have advised the court that they do not desire to press these cross bills.

These actions were commenced on September 19, 1932, within the thirty day period required by section 66 118, Revised Statutes of Kansas 1923.

The several bills alleged diversity of citizenship as to the Cities Service Gas Company, The Western Distributing Company and The Union Public Service Company, and alleged that the orders are confiscatory of plaintiff's property, impair the obligations of their contracts, deny to them the equal protection of the laws, and unconstitutionally interfere with interstate commerce. The bills of the distributing companies also alleged that the governor had directed the attorney general to bring suits to have them placed in the hands of receivers for the purpose of avoiding a judicial review of the orders of August 31, 1932.

An application was made for a temporary injunction. At the hearing thereon, the Commission confessed that the second order made on August 31, 1932, was in conflict with section 66 118, Revised Statutes of Kansas 1923, which prescribes that an order cannot become effective until thirty days after it is entered; and consented that the enforcement of such second order might be permanently enjoined. We granted a temporary injunction against the enforcement of both orders.

The cases were consolidated for trial. Upon the trial the evidence introduced before the Commission was received in [fol. 332] evidence, supplemented by an agreed abstract of such evidence, and by stipulations and other evidence.

Council for the Commission contend that the first order is not subject to any of the constitutional objections urged by the plaintiffs, namely, that it confiscates their property, interferes with their right to contract, and interferes with interstate commerce, because all that it does is to find that the contracts under inquiry are unreasonable,

and the extent of such unreasonableness. They urge that the order does not take any property from the Cities Service Gas Company, that it still may continue to collect the forty cent gate rate, that it does not take any property from the distributing companies, that they may still continue to charge their present rates until a valid order is made requiring them to make a decrease in their charges to their consumers, that it does not require the distributing companies to discontinue the contracts nor to discontinue any payments thereunder, and that such contracts remain in full force and effect.

There are two answers to this contention. The first order, entered August 31, 1932, expressly prohibits the distributing companies from giving consideration to the payments made to Henry L. Doherty & Company and to the Cities Service Gas Company for gas at the city gates in excess of thirty cents per thousand cubic feet "in fixing a rate for the domestic consumer" on and after September 1, 1932. These are two of the important items which enter into the cost upon which the distributing companies' rates are predicated, and the elimination thereof on September 1, 1932, from the rates charged the domestic consumers would have necessarily effected a substantial reduction in rates. Hence, the order is in substance and effect a rate reducing order.

But, if it is only an order adjudging the contracts unreasonable and determining the proper amount which may be [fol. 333] set up for expenditures thereunder as proper operating expense in determining rates for local consumers, and is only a preliminary step in a rate determination, the order is subject to review. Had the distributing companies failed to appeal from such order or seek a judicial review thereof within thirty days from August 1, 1932, it would have become final on September 1, 1932 (sec. 66-118, R. S. Kan. 1923), and the facts therein found would have become res adjudicata, and, in that event, at the hearing under the last paragraph of the second order, the companies could not have defended against an elimination of such items as a part of their operating cost in fixing their rates.

If the construction of counsel for the Commission is correct, the order is plainly an attempt to avoid a judicial review in this court of the matters therein determined, and to

deprive the distributing companies of their constitutional rights. This cannot be tolerated.

The power of a public service commission to inquire into contracts between the company furnishing the service or commodity, the rates for which are under inquiry, and its parent or holding company, has been the subject of judicial inquiry in recent cases. (See Note 1.)

[fol. 334] We think there can be no doubt, under the decision in Smith v. Illinois Bell Tel. Co., supra, and Western Distributing Co. v. Public Service Commission, supra, that the commission has power to inquire into the reasonableness of such contracts. The extent of such inquiry, however, has not been settled.

Counsel for plaintiffs contend that, while the Commis-

[fol. 335] sion may determine whether the contracts are fair and reasonable, and such as ordinarily prudent business men, dealing at arm's length, free from domination

Note 1

In Southwestern Bell Tele. Co. v. Public Service Commission, 262 U. S. 276, the court said:

"The commission is not the financial manager of the corporation and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers."

Again, in United Fuel Gas Co. v. Railroad Commission of Kentucky, 278 U. S. 300, the court said:

"We recognize that a public service commission, under the guise of establishing a fair rate, may not usurp the functions of the company's directors and in every case substitute its judgment for theirs as to the propriety of con-

benefits from the contract and probably could not have secured better terms elsewhere."

But in Smith v. Illinois Bell Telephone Co., 282 U. S. 133, the court said:

"The Western Electric Company not only manufactured apparatus for the licensees of the Bell System, but engaged

of a parent corporation, under the existing facts and circumstances would enter into, or whether they exact an unfair and unconscionable charge for a commodity or service, it may not determine and fix the interstate rate charged for such commodity or service.

It has been settled by repeated decisions of the supreme court that a state commission has no power to fix and regulate contracts entered into by the utility; and common ownership is not of itself sufficient ground for disregarding such intercorporate agreements when it appears that, although an affiliated corporation may be receiving the larger share of the profits, the regulated company is still receiving substantial state interstate gas rates. Hence, a state commission cannot fix the price to be charged for natural gas transported from one state to another and sold and delivered in bulk to an independent distributing company. (Missouri, ex rel., Barrett v. Kansas Gas Co., 265 U. S. 298; Peoples Natural Gas Co. v. Public Service Comm., 270 U. S. 550; Public Utilities Comm. v. Attleboro S. & E. Co., 273 U. S. 83; Pennsylvania Gas Co. v. Public Service Comm., 252 U. S. 23; Public Utilities Co. v. Landon, 249 U. S. 236.)

On the other hand, a state does have the power to regulate the price of gas brought into a state and sold directly to the consumer, because "the business of supplying, on demand, local consumers is a local business, even though the gas be brought from another state and drawn for dis-

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in other large operations, and it cannot be merely assumed or conjectured that the net earnings on the entire business represent the net earnings from the sale to the Bell licensees generally or from those to the Illinois company. Nor is the argument of the appellants answered by a mere comparison of the prices charged by the Western Electric Company to the Illinois Company with the higher prices charged by other manufacturers for comparable material, or by the Western Electric Company to independent telephone companies. The point of the appellants' contention is that the Western Electric Company, through the organization and control of the American Company, occupied a special position with particular advantages in relation to the manufacture and sale of equipment to the licensees of the Bell System, including the Illinois Company, that is, that it was virtually the manufacturing department for

tribution directly from interstate mains; and this is so whether the local distribution be made by the transporting company or by independent distributing companies." (Missouri v. Kansas Gas Co., 265 U. S. 298, 309; Penna. Gas Co. v. Public Service Comm., 252 U. S. 23; East Ohio Gas Co. v. Tax Commission, 283 U. S. 465.)

We are of the opinion that the facts here justify the conclusion that the Cities Service Company, together with the Gas Service Company, the distributing companies, the Empire Gas & Fuel Company and the Cities Service Gas Com- [fol. 336] pany are engaged in a common enterprise, namely, the transporting and furnishing of gas to local consumers; that the Cities Service Company exercises such complete dominion and control over the Cities Service Gas Company and the distributing companies that, under the general rules of agency, the Cities Service Gas Company and the distributing companies are mere agencies or instrumentalities of the Cities Service Company; and that, in substance and effect, the Cities Service Company is, through such agencies, supplying gas to local consumers on demand and is engaged in a local business. If this be true, the Commission had the power to determine the rea-

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that system, and the question is as to the net earnings of the Western Electric Company realized in that department and the extent to which, if at all, such profit figures in the estimates upon which the charge of confiscation is predicated. We think there should be findings upon this point."

Again, in the recent case of Western Distributing Company v. Public Service Commission of Kansas, 285 U. S. 119, the court said:

"The appellant adverts to the fact that in its bill of complaint are included a number of averments not denied by the appellees. In brief these are that the company does be obtained from any other source; that the same rate is being charged to other distributing companies along the lines of the Cities Service Gas Company, and was being charged by another independent pipe line to another city; that an ineffectual effort had been made to find local gas available to El Dorado; and that appellant had attempted to get a lower rate from Cities Service Gas Company, but could not do so. It is urged that as these averments were

sonableness of the charge set up as operating expense for gas at the city gates in fixing the local rate. That could only be done by determining a reasonable return to the Cities Service Gas Company for producing, transporting and delivering such gas at the city gates.

However, if we grant that the Commission can only scrutinize and inquire into the reasonableness of such contracts, we are of the opinion that the same result necessarily fol not own or produce any natural gas; that the only source of supply for the city of El Dorado is the main of the Cities Service Gas Company; that no supply at a lower price can lows. Since the Cities Service Company enjoys a monopoly and affords the only reliable source for supplying gas to the distributing companies, the only method of determining the fairness and reasonableness of the charge at the city gates is to determine the reasonableness of the return to the Cities Service Gas Company on their property used and useful in the business. Any charge in excess of that for gas at the city gates, under the contract between two subsidiary corporations who have the same parent or holding corporation, would be unfair and unreasonable.

It follows that we must determine the value of the property of the Cities Service Gas Company used and useful in

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uncontradicted they constitute, when taken with the facts previously stated, a prima facie case for the reasonableness of the rate charged. This might well be true were it not for the fact of unity of ownership and control of the pipe line and the distribution system. An averment of negotiation and effort to procure a reduction in the wholesale rate means little in the light of the fact that the negotiators are both acting in the same interest—that of the holding company which controls both. All of these facts so averred in the pleadings would be far more persuasive with respect to the propriety of the rate if the parties were independent of each other and dealing at arm's length. Where, however, they constitute but a single interest and involve the embarkation of the total capital in what is in effect one enterprise, the elements of double profit and of the reasonableness of inter-company charges must necessarily be the subject of inquiry and scrutiny before the question as to the lawfulness of the retail rate based thereon can be satisfactorily answered."

the business of producing, transporting, and delivering gas, the amount of its earnings, and a fair return on such property. The case has been tried so that the facts necessary to make these determinations are before us.

[fol. 337] We have made and filed findings of fact and in the footnotes thereto expressed our reasons therefor, and in this opinion will only state the ultimate facts so found.

In determining these facts, we have kept in mind that the findings of the Commission are presumed to be correct. (Blanton v. Belt Line Ry. Corp., 268 U. S. 413, 422; Cotting v. Kansas City Stockyards Co., 183 U. S. 79; Denver Union Stockyard Co. v. United States [D. C. Colo.] 57 Fed. 2d 735, 739), but that, on the question of confiscation, the plaintiffs are entitled to the independent judgment of a judicial tribunal as to the law and facts. (United Railways & E. Co. v. West, 280 U. S. 234, 251; Bluefield W. W. & Imp. Co. v. Public Service Commission, 262 U. S. 679, 689; Ohio Valley W. Co. v. Ben Avon Borough, 253 U. S. 287; Lincoln Gas Co. v. Lincoln, 223 U. S. 349; Crowell v. Benson, 285 U. S. 22, 60.)

In the case last cited, the court said:

"In cases brought to enforce constitutional rights, the judicial power of the United States necessarily extends to the independent determination of all questions, both of fact and law, necessary to the performance of that supreme function. The case of confiscation is illustrative, the ultimate conclusion almost invariably depending upon the decision of questions of fact. This court has held the owner to be entitled to 'a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both the law and facts.'"

The value of the property of the Cities Service Gas Company used and useful in its business of producing, transporting and supplying gas to the distributing companies at the city gates, was found by the Commission to be $73,170,510. We find such value to be at least $82,380,582. The net available annual return from such property was found by the Commission to be $7,161,793. We find such return to be $5,860,327, or a return of 7.11 per cent on the present value of the property.

If the charge made by the Cities Service Gas Company [fol. 338] for gas at the city gates was reduced to thirty

cents per thousand cubic feet, it would result in a reduction of $1,926,145.07 in its net income. This would reduce its return to 4.8 per cent on the present value of its property used and useful in the business.

We are of the opinion that a return of approximately eight per cent upon present values is necessary under present conditions to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties, and that any return substantially lower than eight per cent would be confiscatory. (United Railways & E. Co. v. West, 280 U. S. 234, 252; Smith v. Bell Telephone Co., 282 U. S. 133, 161.)

The undisputed evidence shows that if the distributing companies are compelled to pay forty cents per thousand cubic feet for gas at the city gates and to base their rates to consumers on the price fixed as reasonable by the Commission in its order of August 31, 1932, they will have no earnings in excess of operating expenses to cover depreciation and afford any return on the value of their property used and useful in the business. Upon the trial, it was stipulated that the Cities Service Gas Company could not continue its business without the patronage of the distributing companies.

We conclude, therefore, that forty cents per thousand cubic feet for gas at the city gates is a reasonable charge; that to compel the Cities Service Gas Company to furnish such gas at thirty cents per thousand cubic feet will result in confiscation of its property, and that to compel the distributing companies to pay forty cents per thousand cubic feet for gas at the city gates and permit them to set up only thirty cents thereof in their operating expense, in fixing their rates to local consumers, will result in confiscation of the properties of the distributing companies.

[fol. 339] We have found that the distributing companies in their proof before the Commission failed to establish that the payments of one and three-fourths per cent under the Henry L. Doherty & Company contracts were fair and reasonable, and therefore proper items of expense to be considered in determining local rates for gas.

We set out the applicable provisions of the Kansas statute in Note 2.

Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has built up and maintains a complete organization for the designing, construction, operation, development, and management of public utilities, oil and natural-gas properties. This organization consists of 1,687 employees, among whom are included experienced executives, financial advisers, construction, valuation, electrical and oil and gas engineers, geologists, technicians, rate experts, accountants and operators. Henry L. Doherty & Company also maintains a department for the purchase, sale, promotion and transfer of stocks of the various subsidiary corporations of the Cities Service Company, a foreign oil department, a steamship and tank-car department, an oil-producing and refining department, and a real-estate division chiefly concerned with New York real estate.

As stated in our findings, the activities of Henry L. Doherty & Company embrace many matters not covered by [fol. 340] such contracts, the expense of which cannot properly be charged to the distributing companies.

The evidence before the Commission consisted of proof that Henry L. Doherty & Company is not operated for

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Note 2

Section 74-602c, 1931 Supp., R. S. Kan. 1923, is as follows:

"Showing required for fixing or charging rates. In ascertaining the reasonableness of a rate or charge to be made by a public utility, no charge for services rendered by a holding or affiliated company, or charge for material or commodity furnished or purchased from a holding or affiliated company, shall be given consideration in determining a reasonable rate or charge unless there be a showing made by the utility affected by the rate or charge as to the actual cost to the holding or affiliated company furnishing such service and material or commodity. Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company."

profit, of the services rendered to the distributing companies by it, and of the cost and expense of maintaining The Henry L. Doherty & Company organization. There was no separate proof of the expense which might properly be allocated to the services rendered under such contracts. Therefore, we have concluded that the distributing companies failed to meet the requirements of the Kansas statute by showing in detail the items of service rendered under such contracts and the cost thereof. Furthermore, it was impossible to determine from the evidence before the Commission whether the charge for the services rendered by the distributing companies was fair and reasonable, because the proof was of the total cost and expense of maintaining Henry L. Doherty & Company, which included many activities unrelated to and of no benefit to the distributing companies; and there was no proper allocation of the cost and expense of such unrelated activities.

We are of the opinion that the burden of proof, both under the Kansas statute and under general principles, was upon the distributing companies (Smith v. Illinois Bell Tel. Co., supra, Michigan Law Review, Nov. 1932, pp. 16-24).

Counsel for the Commission contend that the services rendered by Henry L. Doherty & Company are a duplication of the services rendered by the Gas Service Company, and are therefore not necessary or useful to the distributing companies. With this we cannot agree. The Gas Service Company is equipped to render such services only in minor and relatively unimportant matters.

The expense of each distributing company maintaining a separate organization like that of Henry L. Doherty & [fol. 341] Company would be prohibitive. For that reason it is in keeping with sound business principles for it to contract with Henry L. Doherty & Company, or some similar organization, for such services. We therefore conclude that, while the services contracted for are necessary and useful to the distributing companies and that the contracts in that respect are proper, the proof adduced was insufficient to meet the requirements of the Kansas statute or to enable the Commission to determine whether the charges for such services were fair and reasonable.

Certain incidental matters require a limited discussion.

The Commission held that certain gas leases claimed to be held by the Cities Service Gas Company for gas reserves

were in excess of the required reserves, and that they were in fact being held for speculative purposes. The evidence established, and we have found, that the officers and directors of the Cities Service Gas Company, who are men of broad experience in the natural-gas business, in the exercise of an honest and, we think, sound business judgment, determined that such leases were necessary to afford it an adequate gas reserve, and that such leases were acquired and are held by it as bona fide reserves, and not for speculation.

The Commission was not empowered to substitute its judgment for that of the officers and directors of the Cities Service Gas Company as to the amount of leases necessary to afford an adequate gas reserve, in the absence of a showing of abuse of discretion by such officers in that regard. (Southwestern Bell Tel. Co. v. Public Service Com., 262 U. S. 276, 289; State Public Utilities Com. v. Springfield Gas & Elec. Co., 291 Ill. 209, 234, 125 N. E. 891; People v. Stevens, 203 N. Y. 7, 96 N. E. 114, 117; Idaho Power Co. v. Thompson [D. C. Ida.], 19 F. 2d 547, 580; Kansas City K. V. & W. Ry. Co. v. Bristol, 101 Kan. 557, 167 Pac. 1138, 1140; Denver Union Stockyard Co. v. United States [D. C. Colo.], 57 F. 2d 735, 748.)

[fol. 342] Counsel for plaintiffs contend that there should be included in the valuation of the Cities Service Gas Company $3,422,512 to cover initial cost of financing. This item was wholly disallowed by the Commission. We are of the opinion that the Commission's decision was right under the authority of Galveston Elec. Co. v. Galveston, 258 U. S. 388, 397, and Denver Union Stockyard Co. v. United States, supra, p. 742.

We conclude that that portion of the first order of the Commission, made August 31, 1932, that the distributing companies should give no consideration to the payments for gas at the city gates in excess of thirty cents per thousand cubic feet in fixing the rate for the domestic consumer, and the whole of the second order, made August 31, 1932, should be permanently enjoined; and that the temporary injunction against the attorney-general, being no longer necessary, should be dissolved.

Let decrees in accordance with the foregoing be prepared and submitted.

Orie L. Phillips, U. S. Circuit Judge. Geo. T. McDermott, U. S. Circuit Judge.

Hopkins, district judge, dissenting. Opinion later.

[File endorsement omitted.]

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[fol. 343] IN UNITED STATES DISTRICT COURT

FINDINGS OF FACT—Filed Jan. 9, 1933

I

The citizenship and official position of the parties are as stated in the bills of complaint. There is diversity of citizenship in 1646-N, 1644-N and 1645-N, in which cases The Cities Service Gas Company, the Union Public Service Company and the Western Distributing Company are respectively plaintiffs. All of the cases involve a substantial federal question, and in each of the cases there is more than $3,000 in controversy.

II

On July 2, 1931, an order was entered by the Public Service Commission of Kansas, on its own initiative, directed to the plaintiffs herein except the Cities Service Gas Company, finding that the reasonableness of all contracts with, and charges made to, the respondents, by corporations owning the stock of the respondents, and of the contracts between Henry L. Doherty & Company and respondents, should be inquired into; the respondent distributing companies were ordered to show cause why payments made under such contracts, if found to be unreasonable, should not be disallowed as operating expenses. A copy of said order is Exhibit A to the bills of complaint of the distributing companies.

III

Pursuant to such order, extensive hearings were held. The properties of the Cities Service Gas Company, situated in five states, were appraised by engineers for both sides,

and valued by the Commission. The testimony and exhibits comprise many volumes; the expense of the trial, including the appraisement of the engineers, exceeded $300,000. On July 20, 1932, the Commission found that the payment of 13½ per cent of gross revenues made by the distributing companies to Henry L. Doherty & Company were unreasonable; that any rate paid by the distributing com- [fol. 344] panies to the pipe line company (the Cities Service Gas Company) in excess of 29.5 cents per thousand cubic feet for natural gas delivered to the mains of the distributing companies was unreasonable.* The distributing companies were ordered (1) to cease setting up on their books the payments of 13½ per cent to Henry L. Doherty & Company, and any payment for gas in excess of 29.5 cents per thousand cubic feet, and (2) to give no consideration to any such payments in fixing their rates to the domestic consumers, and (3) to reduce their rates to the consumers proportionately, pending a final determination of their rates; notice was given to show cause why such reductions should not be made permanent. A copy of such findings and order, with an elaborate supporting opinion, are attached to the bills by reference.

IV

A petition for rehearing on fifty one grounds was filed, and allowed as to one. Upon rehearing, a slight addition was made to the value of the properties of the pipe-line company, and the city gate rate was increased from 29.5 cents to 30 cents per thousand cubic feet. The order entered in July was again entered, this time as two orders; part (3) of the July 20th order, requiring a reduction in rates pending further hearing, was incorporated in a separate order. Upon the hearing of the application for a temporary injunction, counsel for the Commission confessed that part of the order to be invalid.

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*The city-gate rate is referred to throughout the record, and in these findings, as the "40-cent rate." That is the usual charge per thousand cubic feet for gas delivered to the mains of the distributing companies; local conditions lowered that rate to certain cities supplied by the pipe-line company, bringing the average down to the 39.5 cents referred to in the opinion and order of the Commission.

V

Except for qualifying shares, the common stock of the distributing companies is owned by the Gas Service Company, the stock of which in turn is owned by the Cities Serv-
[fol. 345] ice Company. The common stock of the Cities Service Gas Company is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. The Empire Gas & Fuel Company has a preferred stock issue outstanding in the hands of the public. Henry L. Doherty & Company is Henry L. Doherty, who owns thirty five per cent of the voting stock of the Cities Service Company. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of the Cities Service Company. The distributing companies do not deal at arm's length with either the Cities Service Gas Company or Henry L. Doherty & Company.

VI

The distributing companies, plaintiffs, are engaged in the distribution and sale of natural gas to domestic and industrial consumers. They operate in 128 cities and towns in Kansas. Their only dependable source of supply is the other plaintiff, the Cities Service Gas Company. Except for a few local gas fields of uncertain life, the distance of the gas fields from the localities served, and the cost of pipe line construction, are such that the Cities Service Gas Company has a practical monopoly on the sale of gas to the distributing companies. There is no agreement between the Cities Service Gas Company and the distributing companies as to the amount of gas that will be purchased; the oral agreement is simply that the pipe-line company will supply the present needs of the distributing companies at 40 cents per thousand cubic feet delivered to their mains.

VII

Prior to 1910, and during the years since then, Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has built up and now maintains a complete organization for the design, construction, operation
[fol. 346] and development of public utilities, oil and natu-

ral gas properties. This organization is composed of experienced executives, financial advisers, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technicians, experts, accountants and operators. There are approximately 1,687 employees.

The same organization maintains departments for the purchase, sale, promotion and transfer of stocks of the various companies allied with the Cities Service Company; a foreign oil department; steamship and tank car department; an oil production and refining department; a real estate division chiefly concerned with New York real estate.

Each of the plaintiffs has entered into a contract with Henry L. Doherty & Company, by which the latter agrees to furnish the following services, subject to the control of the board of directors of the plaintiffs:

"I. Personnel. In so far as your corporation may desire, it is proposed to supply you with experienced executives and operators necessary for your business.

"II. Executive service. Our staff of executives, financial advisers, engineers and accountants will advise and assist in franchises, rates, matters of public relations, and all matters of insurance, supervise expansion of territory and business, acquisition of additional properties, etc.

"III. General accounting services. Our accounting department will periodically audit the books of your corporation and generally advise in accounting problems and in the developments in accounting practices and procedure, and furnish the services of certified public accountants where special audits are required.

"IV. Statistical services. Our statistical department will supply comparative statements of operating results of the various companies under our supervision and will also supervise or furnish statistical reports to financial institutions, government bureaus, and similar organizations.

"V. Purchasing services. We will give you the benefit of the services of our purchasing department with regard to [fol. 347] the purchase of equipment, supplies, generally advise as to the desirable equipment, etc.

"VI. Designing and construction engineering. Our engineering staff will be available at all times to carry out all preliminary investigations requisite to determining the advisability of any proposed construction, will check the

details of engineering design, perform engineering work where requested, and generally check the efficiency of your plant.

"VII. Financial services. The financial department will provide plans for financing and for funds for capital requirements, including construction and additions to properties and acquisition of new properties; for the refunding of maturing obligations; will act as paying agent for coupons and dividends, and assist in the arranging of bank loans. Also the financial department will furnish your corporation with a budget system for the advanced determination of financial requirements and operating results.

"VIII. Securities department. The securities department will provide plans for the sale and distribution of various securities, and will formulate and carry out campaigns for sales under customer ownership plans, etc.

"IX. Valuation. The valuation department will, when required, prepare inventories and appraisals of property, and will advise as to experts who may be required to testify in valuation cases, and will generally assist in the preparation of the same.

"X. Tax department. The tax department will prepare or supervise the preparation of federal and other tax returns and generally keep in touch with taxation problems.

"XI. New business department. The new business department will serve in the purchase and sale of appliances and equipment for resale, the determination of sales policies, promotion programs and sales personnel, in research and laboratory tests on domestic appliances, etc.

"XII. Technical and research department. The technical and research department will furnish a consulting service on all technical problems encountered by your corporation.

"Compensation. For the above services your corporation will pay as follows:

"1. A management fee equal to one and three-fourths per cent (1¾%) of its gross revenues, after deducting intercompany sales for resale.

[fol. 348] "2. An engineering fee equal to five per cent (5%) of the cost of construction.

"3. For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made.

"In addition, your corporation will pay the expenses, disbursements and reasonable per diem charge for our representatives while at the properties of your corporation or traveling for it on special matters."

Payments received under these contracts are paid over to Cities Service Company, which in turn pays all the expenses of Henry L. Doherty & Company, without profit to Henry L. Doherty. The 1¾ per cent payment is not made on intercompany sales; that is, the Kansas consumer pays the 1¾ per cent but once.

## VIII

The Gas Service Company, with offices at Kansas City, Mo., renders certain services to the distributing companies, for which a payment is made that is not here under review. While the same type of service is rendered under each of such contracts, there is no unreasonable duplication of service. Henry L. Doherty & Company furnish services which the Gas Service Company is not equipped to furnish. For example, the counsel and engineer employed by Gas Service Company can and do adequately handle the routine matters involving rates and service that arise in ordinary operations; they are not equipped to handle matters of the magnitude of this litigation; in such cases, the engineering and legal staffs of Henry L. Doherty & Company are employed. We find that this contract places at the disposal of the distributing companies engineering, legal, accounting, geological and business services of value, and of a character and extent which could not as economically be availed of by separate distributing companies or by any [fol. 349] small group of them; that similar contracts are made by other public utilities with similar organizations, such as Ford, Bacon & Davis, and Stone & Webster; that the propriety of such contracts is for the owners of the companies to determine.

IX

The activities of Henry L. Doherty & Company embrace many matters not covered by the 1¾ per cent contract, the expense of which is not a proper operating charge of the distributing companies. These activities are: the promotion, sale, and transfer of securities of the Cities Service Company and its affiliates. No securities of the distributing companies have been marketed by Henry L. Doherty & Company, and if they are, the contract provides for a separate fee for such services. The production, sale and transportation of oil, and the handling of New York real estate, are unrelated activities. The record discloses no reason for these distributing companies maintaining a London office.

The following activities of Henry L. Doherty & Company are or may be of direct benefit to the distributing companies:

Activities tending to increase the consumption of natural gas, by advertising and by development and marketing of gas-burning appliances; the geological department, the technical and research division; the tax, valuation and rate divisions; the purchasing department; the public utilities operating department; the department dealing with the training of personnel; the natural gas department; the corporate records department; the legal, engineering, accounting, auditing, finance and construction divisions.

X

The record discloses that the expenses of Henry L. Doherty & Company exceeded its receipts, over a ten-year period, in the amount of $1,768,440.26, the deficit being made up by the Cities Service Company. The expenses for [fol. 350] one year are classified, and from that classification a rough approximation of the expenses properly chargeable to the natural gas business is possible; something less than one-half of the 1931 expenses appears to have been incurred in activities not contemplated by the contract and not properly chargeable to operating expenses; certain large items, such as executive and office service, include the expense of both related and unrelated services. But the receipts are not classified. The utility business pays 1¾ per cent; the oil business 1 per cent; the

securities business apparently pays nothing directly, except that Cities Service Company makes up the deficit. But whether this is a fair division the record does not disclose, except that the deficit, over a ten year period ending in 1930, has been about 7 per cent, while the expenses of the securities business for 1931 were close to 30 per cent. It is therefore impossible to tell, from this record, anything about the pivotal question of whether the payments made by the distributing companies bear any fair relation to the expenditures properly made on their behalf. We cannot, therefore, find whether 1¾ per cent is too much or too little; it is probable that, until some segregation is made of departments, and perhaps a segregation of expenses within some of the departments, no accurate finding on this point can be made. If the entire 1¾ per cent is eliminated, the reduction of the average gas bill would be about ten cents a month. The record discloses that a part, at least, of such payment is proper. A finding of the amount thereof should be made, in the first instance, by the Commission.

XI

We find that it is of value to the distributing companies to have available a central organization equipped to render services of the character described by the contract, on demand; that the payment of the per diem charge, the per [fol. 351] centage on construction contracts, and the fee for the sale of securities, does not meet the expenses of such service, since much of the service is rendered without such specific charges. That whether such contract is advisable is for the officers of the distributing companies to determine. That the actual expenses of such services, if fairly allocated, is a proper operating charge.

We find it is not practicable to allocate with precision the cost of such general services to each distributing company, except so far as it is now allocated by the per diem and per cent charge in the contract. We find it practicable to segregate the cost of the services rendered to the public service companies engaged in selling gas, and perhaps electricity, to the public, from the cost of services rendered to companies engaged in the oil business, and from the expenses incurred in the promotion and sale of securities. The consumers of natural gas and electricity have no in-

terest in the oil or stock business, and such private business ought not to be thrown into a common pot with the business of serving the public, the expenses of all hopelessly intermingled, and then proportioned back to the public by those interested in the private business.

## XII

The Cities Service Gas Company was organized in 1926. It took over the physical properties of five pipe line companies, having a plant investment account, at the time, of $[illegible]. These pipe line companies served many communities in Oklahoma, Kansas and Missouri. The companies taken over were integrated, so that gas could be run from the mains of one system into that of another, and the supply thereby made more dependable and economical. Natural gas had long been used for lighting and cooking in most of these cities and towns. Years ago gas had been freely used for heating, but the uncertainty of the [illegible] supply, caused in part by lack of capacity of the wells to meet the peak demands and in part by the frailties of the pipe line system, had driven the ordinary householder back to coal. The discovery of the extensive and prolific gas field at Amarillo, and later at Hugoton, Kansas, removed the first obstacle; large sums expended in new mains and in repair of old ones largely removed the second. The supply becoming again dependable, a vigorous campaign was waged for household heating and for industrial uses to absorb the excess in off peak seasons. The Cities Service Gas Company now has an adequate and dependable supply of gas, available at all times at the city gates. The Cities Service Company acquired the distributing companies in order to insure adequate service to the ultimate consumer, on the theory, doubtless, that a chain is no stronger than its weakest link. The service to the public is now sufficient and efficient. While these improvements in service were being made, electricity supplanted gas for lighting and is making serious inroads on the cooking, while fuel oil is proving a formidable competitor for heating. The original cost, or prudent investment, in the pipe line company's properties is somewhat obscure; the properties were acquired by a merger of other companies, whose original investment accounts cannot be

thoroughly checked. The probabilities are that the book cost of the properties is around $90,000,000. The system consists of 4,400 miles of pipe lines, 11 compressor stations, and 1,225,000 acres of gas leases, and gas wells on a part thereof.

## XIII

There is no substantial dispute as to the inventory; the disagreement is over the present values of the properties. The valuations made by engineers for both sides, and by the Commission, is on the basis of cost of reproduction new, less accrued depreciation. The present values are, on the extensive constructions of the last few years, less than the prudent investment therein. Both engineers arrived at [fol. 353] the present per cent condition by inspection, although the amount of properties inspected differed somewhat. The engineers for the plaintiffs value the properties at $105,000,000; the engineers for the Commission, and the Commission, at $73,000,000. Approximately $22,000,000 of this difference is in four items gas leases, going concern value, cost of financing, and interest during construction. The remaining difference grows out of differences in valuations of the numerous items in the inventory. While this court has made an independent investigation of the facts, it has done so with the knowledge that the Commission had the benefit of hearing the witnesses, and that there is a presumption that their findings are correct. Unless, therefor, the record discloses some substantial reason to the contrary, the findings of the Commission have not been disturbed. The Commission apparently gave little or no weight to the factor of original cost, although when present values were higher than cost, great weight was accorded that factor by Commissions generally. We have found it unnecessary to explore the question of what weight should be given to that factor.

In the following findngs of value, the Commission's finding is adopted, because presumptively correct, except where there is an explanatory note.

## XIV

The properties of the Cities Service Gas Company, used and useful in the public service as of September 1, 1931, are as follows:

| | | |
|---|---|---|
| 1307 | Production—Right of way* | $64,778 |
| 1327 | Transmission—Right of way | 1,915,427 |
| 1310 | Production—Field measuring station structures | 35,909 |
| 1311 | Production—Other Structures | 47,876 |
| 1312 | Production—Gas Well Construction* | 1,294,710 |
| 1313 | Production—Gas Well Equipment | 658,439 |
| 1314 | Production—Field Line Equipment* | 3,523,176 |
| 1315 | Production—Field measuring station equipment* | 265,746 |
| 1332 | Transmission—Measuring station equipment | 759,625 |
| 1316 | Production—Drilling and cleaning equipment | 27,908 |
| 1317 | Production—Other Equipment | 1,333 |
| 1325 | Transmission—Land* | 147,202 |
| 1328 | Transmission—Compressing Station Structures* | 1,515,662 |

[fol. 354]

| | | |
|---|---|---|
| 1329 | Transmission—Measuring Station Structure | 133,310 |
| 1330 | Transmission—Other Structures | 113,341 |
| 1331 | Transmission—Compressing Station Equipment* | 8,463,835 |
| 1333 | Transmission—Line Equipment* | 40,232,331 |
| 1334 | Transmission—Other Equipment | 5,633 |
| 1376 | General—Other Land | 3,655 |
| 1379 | General—Other Structures | 94,687 |
| 1380 | General—Office Equipment | 106,035 |
| 1381 | General—Store Equipment | 1,805 |
| 1382 | General—Shop Equipment | 23,084 |
| 1383 | General—Stable Equipment | 568 |
| 1384 | General—Garage Equipment | 81,448 |
| 1385 | General—Laboratory Equipment | 8,202 |
| 1386 | General—Telephone and Telegraph System | 415,070 |
| 1387 | General—Tools and Implements | 44,979 |
| 1388 | General—Other Equipment | 21,832 |
| | Engineering and Superintendence during Construction* | 3,321,250 |
| | Preliminary and Organization Expense* | 500,625 |

| | |
|---|---|
| Administration and Legal Expense during Construction | 350,350 |
| Miscellaneous Construction Expenditures | 700,700 |
| Taxes during Construction | 875,171 |
| Interest during Construction* | 4,471,934 |
| Working Capital | 775,000 |
| Materials and Supplies* | 628,675 |
| Gas in Line | 22,000 |
| Going Concern Value* | 5,000,000 |
| Gas Leases* | 5,727,272 |
| Rate Base | $82,380,583 |

1307-1327. (Mr. Black was the engineer for the Commission; Mr Hamilton for the plaintiffs. Both are engineers of standing.) The Commission allowed $1.40 a rod for right of way. It used $1.08 as a basis, that figure being the average cost, as shown by the books of the company, of 31 per cent of its rights of way. To this the Commission added 22 cents per rod for expense of acquisition, and 10 cents a rod for abstracts and recording fees. The evidence clearly developed that the figure of $1.08 did not purport to represent all of the costs, and it is not a dependable figure. The most dependable evidence is that of the man who negotiated for these rights of way during the past four years. His offering price, to all landowners, was 50 cents per rod for the land, and 50 cents per rod for damages; sometimes he paid as much as $2 per rod for the land alone; the average damage paid was 65 cents. He did not state the average cost for the land, but it cannot be assumed that he acquired all of it at his offering price. It should not be figured lower than 65 cents, the average [fol. 355] he paid for damages for which his offer was likewise 50 cents. These items make $1.30 per rod paid the landowner; adding to that the 32 cents allowed by the Commission for overhead, gives the figure of $1.62, which we have used. The company's figure of around $3 includes aerial surveys, which were not used, and if used, probably would have been worth their cost in a saving not reflected in its present valuation. Apparently the company also included certain construction costs elsewhere accounted for.

1312-1313. We have added two items to this joint ac-

count. The Commission deducted $57,235 from its engineer's valuation on a purely legal ground. It appears that in the Craig and Augusta fields the company uses dry holes, or played out wells, for storage; that is, excess gas from producing wells is turned into the dry holes, and the gas thereby stored for future use. It is not denied that the wells are properly used for storage, and for a public purpose; the claim is that the landowner has the property interest in the hole in the ground. Upon the trial before this court it was conclusively proven that the company has entered into gas leases, with royalties paid in advance, for the use of these wells. Its rights thereto are the same as in producing leases. The assumption of fact made by the Commission is erroneous; the legal conclusion need not be examined.

The other item is $84,318 growing out of the cost of gas-well construction. The company's figures were considerably below actual cost, and below the cost of adjacent wells drilled by other companies to the same depth. The engineer for the Commission omitted certain items in his calculations, which may account for his figures being so much below the actual cost of such construction. The Commission's figures are so far below the cost of these wells, or any other well in the vicinity, that they approach the arbitrary.

Counsel for the Commission suggests that the Commis- [fol. 356] sion's valuation is too high, because the per cent condition was computed on a straight line basis, whereas, in fact, as he says the gas wells depreciate more rapidly during their early years. None of the witnesses support this theory; it introduces a highly speculative element into an already troublesome problem; it is of no practical significance in this case, because the number of wells is large and of varying ages, and any theoretical error as to a single well is leveled out by the law of average.

1314. We have added $397,017 to this account. The Commission adopted Mr. Black's estimate, which was based on assumption that field lines were buried, on the average, to one-half the depth of main lines. The company's valuation was based upon the facts. Black testified his figures would have been more accurate if he had had time to gather the

facts. It clearly appears, also, that field lines are more expensive to construct than main lines; they are in smaller units; more hand labor is involved, and more connections are necessary; also the cost of field lines cannot be decreased by taking advantage of topograph, as may generally be done with main lines. The company's figures are strongly buttressed by an analysis of actual cost of field lines utilizing 20,600 tons of pipe. The assumptions of the Commission and its engineer cannot stand against the facts.

1315 1332. These accounts are treated together, and we find nothing from which to resolve the conflict between the engineers. The Commission rejected Hamilton's value because without supporting data; on rehearing the data was furnished, several volumes of it. It still leaves the conflict. We therefore use the Commission's valuation.

1325. We have added $2,000, the value of the land at the Hogshooter compressor station. The Commission eliminated this land, and the structure and equipment, on the [fol. 3574] ground that it was an abandoned station. The station is an old one, and has not been in use since 1925, because the gas fields supplying it were exhausted, and it was not so located as to serve other fields. In February, 1931, it was returned for taxes as an abandoned structure, at junk value. Since that date new gas fields have been discovered, and it is undisputed that the station is now strategically located, and plans and requisitions have been prepared to make the necessary alterations to put it back into immediate service. This undisputed evidence, corroborated by the physical facts, cannot be ignored because a tax return was made that at an earlier date it was abandoned. It is not now in service, except as an emergency station, but it is a component part of the system as it now exists. If eliminated now, a readjustment of the rate base would be necessary as soon as the work now requisitioned for is completed. We have restored this station to the rate base, using the valuation of the Commission's engineer.

1328. We have added the Hogshooter structure at Black's value of $49,560. We have not added the compressor stations at Owasso or Hominy. There is a difference of about $700,000 in the value of the structures at other compressor stations. Each engineer is corroborated by

contractors who estimated the cost of reproduction. The engineers and contractors testifying are all reputable and capable men. We therefore hold that the presumption of correctness attaching to the finding of the Commission has not been overcome.

1331. We have added the Hogshooter equipment at Black's valuation.

1333. The difference between the engineers' valuations of this item is about $4,000,000. The dispute narrows down to three items. (1) The Commission found the property to be in 90.1 per cent condition. The company asserts it to be in 92.93 per cent condition. The Commission's finding is supported by the testimony of its engineer and a con- [fol. 358] sulting engineer called by the company. We approve the Commission's finding as to per cent condition. (2) The cost of rock excavation. There was a dispute among the experts, but the Commission's finding is supported by the testimony of its engineer and a contractor who had done much of this work. Elaborate comparisons of costs of selected lines are introduced to show the error in the Commission's cost figure. But the results depend largely on the lines selected. While not entirely satisfied with the figure used, we are not disposed to disapprove the finding as to the cubic yard cost. (3) There is a difference between the engineers as to the amount of rock excavation in the lines. After the hearings before the Commission, engineers for both sides drilled a hole every quarter of a mile along a main 125 miles long. That extensive investigation developed that the percentage of rock excavation was 20.94 per cent instead of 10.46 per cent used by Black. If overcuts are included, the percentage is 28. We are inclined to believe that overcuts should be excluded; it is probable that contracts for trenches would be predicated on the trench debt, and would not call for overcuts caused by the inability to blast to a neat line. This additional evidence convinces us that Black's estimate of the amount of rock excavation is too low. His estimate on the line used for the test was 24,000 yards; Hamilton's was 72,482 yards. The test showed, on Black's own figures, exclusive of overcuts, 46,790 yards. The subject is not capable of exact proof, but we are of the opinion that Black's amounts of excavation should be materially increased. Mr. Hamilton's valuation of rock excavation is $4,211,120; Mr. Black's

$1,270,115, of which $1,154,503 is in this account. Applying Black's price to an increased amount indicated by the test, results in an increase of this item from $39,432,331 to $40,232,331.

Engineering and Superintendence is stipulated by the [fol. 359] parties to be 5 per cent of the value of the properties excepting accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387, and 1388. The parties have stipulated that this and other overheads should not be depreciated. Accordingly we have computed overheads by applying the Commission's percentage to the undepreciated values of the property, using $66,425,000.

Preliminary and Organization Expense. We adopt the Commission's finding of ¾ per cent of the values of the physical properties; and for Administration and Legal Expense, ½ per cent on physical values including engineering; for Miscellaneous Construction Expenditures, 1 per cent, on same values. (See note.)

Interest During Construction. The Commission used a rate of 6 per cent; the company, 8 per cent. It is customary to calculate this item at the prevailing rate charged a person with good credit for temporary advances, which is now 6 per cent. This throws upon the borrower, the owner of the property, the hazard of the borrowed money during the construction period, which must be considered. Two per cent is a reasonable allowance for that hazard, but it is customary and preferable to make this allowance as a part of Going Concern Value. The parties have agreed that this item, as well as taxes, should not be depreciated. We have taken the Commission's figure, increased by 6 per cent on the difference in values found, approximately $200,000.

Materials and Supplies. Commission's figure plus its allowance of $119,275 on rehearing.

Going Concern Value. Mr. Hamilton's estimate of going concern value is $8,898,532. Ford, Bacon & Davis valued this item from $8,500,000 to $9,000,000. The engineer for [fol. 360] the Commission valued it at $3,820,000. The

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Note.—We accept the Commission's finding, instead of the stipulation of the parties, because the Commission's finding is in accord with the record, and there is an acknowledged error in the stipulation.

Commission allowed $2,000,000. Counsel for the Commission urges that nothing be allowed.

That such a value exists is acknowledged by all engineers and appraisers, and is a matter of common knowledge. That allowance therefor cannot be denied because of difficulty in evaluation, is settled by decisions of the Supreme Court of the United States and of the Supreme Court of Kansas. Many items enter into it. There is a value to records that have been built up, and to a personnel that has been trained. The period of construction was two years. Physical deterioration went on during that period when there were no earnings to offset it. The owner's money was embarked in a hazardous enterprise during the construction period; the Commission allowed only 6 per cent for interest during construction on the theory that an owner, with good credit, could borrow money at that rate. But the owner should be compensated for the risk involved in putting his credit back of the enterprise. If 8 per cent is a fair return on moneys embarked in this business, as we elsewhere find, that hazard was present during the construction period. The difference between 6 per cent interest during construction and an 8 per cent return in a business venture during construction, is $1,450,645, based on the Commission's valuation. During the construction period, there are no revenues, and depreciation and return (less interest during construction) must be capitalized in going concern value. After construction is completed, and some business is attached, there is an idle investment until the available business is fully attached, even under the most efficient management. It would be foolish, of course, to construct a pipe line capable only of taking care of the needs of to-day, with no provision for the reasonably anticipated needs of to-morrow. The Commission recognized this in another part of its opinion, when it stated:

[fol. 361] "Further, as pipe line extensions were developed, they necessarily were not fully productive until the volume of sales had been built up to the capacity of such extension. A large proportion of the investment each year was unproductive, although the investment has been included in the plant investment values included in the above, and will be included in the future. This discussion relative to idle plant is merely for the purpose of illustrating that the company has been earning a high return not only on

its production property but on its idle and non productive property."

The Commission's theory that rates for the future should be discounted because of the profits of the past is not sound law. Values cannot be increased by capitalizing past losses; (Georgia Ry. v. R. R. Comm., 262 U. S. 625, 632) the corollary that they cannot be decreased by reason of past profits, is equally well settled. (Board of Commrs. v. N. Y. Tel. Co., 271 U. S. 23, 32.) Counsel for the Commission assume, contrary to the finding of the Commission, that the business existed when the lines were constructed. The town existed; the distributing companies existed; there was a market for some gas. But, like every other utility, the market had to be and was developed. Vigorous campaigns, in part successful, have been and now are being carried on to develop the market, particularly for house heating and for industrial gas to utilize the surplus in off peak periods. It is no answer to say that these campaigns are carried on by the distributing companies; no matter who developed the market, the fact is, as testified to by the engineer for the Commission, and as found by the Commission, a part of the plant was necessarily idle while the market was being developed. The Commission's engineer testified:

"I have taken as the best measure of certain items of that going value the company's operating experience, and briefly I have allowed in arriving at this figure used herein, $15,000.00 for the books and records of the company, I have allowed $1,020,000.00 for organization of the operating company, that is the organization of the company, and I have allowed interest and depreciation on idle plant, plant [fol. 362] that would be idle during the period this company is acquiring its business, that is between the end of the construction period and the time all business is attached, in the amount of $2,784,645.00, added to the two other amounts of $15,000.00 and $1,020,000, gives $3,819,645.00, which I have applied as $3,820,000.00."

While Mr. Black allowed depreciation and return on idle plant while the company was acquiring its business, in the amount of $2,784,645, no similar allowance apparently was made during the construction period. The difference between 6 per cent interest allowed and an 8 per cent return is $1,450,000. The parties agree on the Commission's fig-

are of 2.90 per cent annual allowance for depreciation. Allowing half of that for the two-year construction period, adds approximately $2,715,000. Without undertaking any precise evaluation of this intangible asset, it is difficult to see how it can be fairly approximated at less than $5,000,000 which is about 5 per cent of the tangible values, a much lower percentage than the percentage customarily allowed.

Cost of financing, valued by the company at $3,422,512 was disallowed by the Commission; we approve, on the authority of Galveston Elec. Co. v. Galveston, 258 U. S. 388, and Denver Union Stockyard Co. v. United States, (D. Colo.) 57 F. 2d 735, 742, and cases there cited.

Gas Leases. The company owns the gas rights in about 1,261,000 acres, of which 42,297 acres are developed; 196,170 acres proven; 25,667 are in probable territory; and 998,287 acres are classed as of prospective value only.

Many experienced witnesses, testifying for the plaintiffs, valued these leases at figures, the average of which is $12,914,189, of which $1,996,574 represents the 998,287 prospective acreage. Mr. Holl testified for the Commission as to values; he was a practical geologist and oil man, with [fol. 363] no personal knowledge of the fields in question; and no particular experience with gas leases. His testimony was predicated on a trip he made to the fields for the purpose of testifying, and inquiries made on that trip. He valued the leases at about one third of the company's value. The Commission valued them at $3,279,237 of which $998,287 was for prospective acreage. The Commission valued the Amarillo holdings at $4,281,894; the Hugoton holdings at $556,116. The cost of the leases, after deducting those bought for the Texoma Company, was $5,727,272.

The Commission excluded all but 71,267 acres from the rate base. The holdings of the company at Amarillo alone are 94,820 acres. The acreage allowed is valued by the Commission at $2,874,390. The Commission arrived at this result by finding the amount of gas left in the Amarillo holdings, based upon the estimate of geologists; it deducted from the company's requirements, gas now being purchased by the company from other producers; and found that the gas in the acreage allowed would serve the customers for 22 years.

The Commission found that the remaining leases were acquired for speculative purposes, a finding based upon

one fact: the Texoma Company was formed by the Cities Service Gas Company and other interests to build a pipe line to Eastern states; leases were acquired by the Cities Service Gas Company for its affiliate, and later transferred to it. On the other hand, in this court, is the uncontradicted sworn statement of responsible officials that all the acreage was acquired as gas reserves for this pipe line. There is also the significant circumstance that not a single lease, acquired for that purpose, has been sold. We hold therefore, that these leases were acquired, and are held, in good faith, for this pipe line, and that the findings that they are held for speculative purposes is contrary to all the evidence.

We further find there was error in eliminating these leases from the properties of the company because the company is now contracting some gas, and conserving its [fol. 364] own. The first duty of the company is to see to it that its patrons have an adequate supply of gas. To insure this, it must own the gas. Contracts for gas are well enough when gas is plentiful, but when the shortage comes, contracts are not adequate safeguards. Broken contracts will support verdicts for damages, but they will not heat the houses nor cook the breakfasts of the patrons in Kansas. The company has not only the right, but is under the duty, to own enough gas to meet the needs of its customers.

Who shall determine what reserves are adequate? A Commission, with no moneys invested, or the owners of this pipe line which, without gas, is worse than useless? Within the limits of reason, undoubtedly that determination must be left with the owners. Perhaps they have been over-cautious, but if error is to be made, it should be on the side of ample reserves. The owners of this property had seen the gas exhausted from field after field; they had seen their customers lost because the supply had failed; they had seen fields of great promise belie their expectations. They had seen geologists wrong before. In recent years they had seen the state prorate the taking of gas. The Commission's figures are predicated on a 20 per cent recovery; within two weeks of its order, the Texas Railroad Commission cut this to 4 per cent. What the future may hold, by way of state action, no one knows. We cannot say the owners did not, in good faith, acquire this acreage to protect their great investment and to insure their patrons a de-

pendable gas supply. They invested around $4,500,000 in 200,000 acres in proven or probable territory, and about a million more in a million acres in prospective territory. Upon this five and a half million investment depends the entire value of $75,000,000 of pipe lines and many more millions in the properties of affiliated distributing companies. The Hugoton field is not now connected with the pipe line; but it is a field of great potential supply, is fa- [fol. 365] vorably situated, and the investment therein is not large. We find that all the acreage owned is used and useful in the public service.

The value of it is problematical, as is true of all gas properties. If the Amarillo field stands up, it is probably worth the value placed on it by witnesses for the company; if it stands up, then that field is adequate for the needs of twenty years; it may not stand up, and the company acquired Hugoton and other acreage against that eventuality; if it does not, it is not worth so much. Its value depends upon a future market, and on the actions of state commissions. The overwhelming weight of the competent evidence sustains the valuation of the company, around $12,000,000. That is about twice its cost. For the purpose of this case, and upon the authority of United Gas Co. v. Railroad Commission, 278 U. S. 320, we have put the gas leases in at cost. The figure is arrived at by subtracting from the cost of all the leases, the cost of those transferred to Texoma, which leaves the cost of those now held.

## XV

Equally efficient substitute. The chief engineer for Ford, Bacon & Davis testified that the present cost of a pipe line from the gas fields at Amarillo to the cities served by the Cities Service Gas Company, together with the cost of acquiring adequate gas reserves, would be $91,500,000. That in making this estimate he had assumed that the lines could be constructed as the crow flies, and he did not take into account the actual topography of the country; that the lines were designed as cheaply as could be, and that such a system would not furnish the same quality of service as is now furnished by the present pipe line. Applying the 90 per cent condition of the present system to the physical properties of this hypothetical substitute, would reduce this

figure approximately $7,000,000 (computing $70,000,000 as cost of depreciable properties in hypothetical line), or a present value of $84,500,000.

[fol. 366] XVI

The revenues which can reasonably be anticipated from the properties of the Cities Service Gas Company under the present rates, are as follows:

| | | |
|---|---|---|
| Annual net operating income* | | $8,401,680 |
| Depreciation of physical properties, at agreed figure of 2.96% | $1,966,180 | |
| Rentals on nonproducing leases* | 329,917 | |
| Dry hole expense* | 174,747 | |
| Depletion of producing leases (agreed) | 70,509 | 2,541,353 |
| Net available for return, or 7.11% | | $5,860,327 |

Operating income. Except for two items hereinafter noticed, operating expenses are not questioned. The record discloses operating income for the two years ending June 30, 1931, and June 30, 1932; and also for the year ending December 30, 1930, but this year involves a six months overlap into the June 30, 1931 year, with no way to apportion it. We have accordingly taken the two separate years shown. The income for 1932 was $880,000 short of 1931. We agree with the Commission that 1932 should not be taken as a test year, for it marks, it is hoped, the low of the depression through which we are passing. The 1932 figure of $7,861,516 includes an item of $52,297.13 paid under the 1¾ per cent contract, which the Commission disallowed. It also includes an item of $50,000 being a portion of rate case expense of $250,000, amortized to that year. The Commission taxed $66,936.08 as costs to the respondents. The Commission, not challenging the amount, deducted it as a non-recurring expense. But the court records show that rate cases constantly recur. The city-gate rate for gas, serving the cities involved in this case, has been almost constantly in court for nearly twenty years. Extraordinary rate expenses should be amortized and allowed for the reasons set out in Denver Union Stockyard Co. v. United States (D. C. Colo.), 57 F. 2d 735. The $50,-

000 calculated in but one of the test years, is an estimate that $25,000 a year of such expense may be expected. We [fol. 367] have averaged the two years shown (adding the 1¾ per cent payment to each year) and adopted $8,401,680 as the anticipated revenues for the future.

The Commission still further increased this, by assuming that the income of 1931 was earned upon a lesser investment in the properties; accordingly, the Commission deducted from its value as of September 1, 1931, net additions to capital as disclosed by the company books from January 1, 1930, to September 1, 1931. But this is shown to be inaccurate, because additions were not charged to capital until long after the addition was in service; a lag of from one to three years was customary, in order to close up all claims growing out of a particular job. During 1931 there was almost no construction; there was some during 1930, but part of that was to replace existing facilities. There is evidence that there were not to exceed $2,000,000 additions to plant in the test period; and this would be more than offset in the decline of values between 1930 and the date of the valuation. The properties upon which a return is allowable are those actually in public service at the time of the valuation, and not an average of values theretofore existing. Income for the past, used as a guide for the future, should be figured against property in service when the income was earned; but the facts are, without contradiction, opposed to the Commission's assumption in this regard.

To this income the Commission added a sum for construction credit which it is now stipulated is in error; and also an item of $23,310 for income tax accruals in the calendar year of 1930, the origin of which is not clear. Income tax is an operating expense. Galveston Electric Co. v. Galveston, 258 U. S. 388. This appears to be an excess accrual over the amount finally determined to be owing for the year; if so, it means the operating expenses for the year are too high; but the record does not show whether it is already [fol. 368] deducted in arriving at the stipulated "net income." If it was not deducted, the stipulated figure is not "net income" as it says it is. The item is not of particular significance; only half of it is applicable to the last six months of 1931; and averaging that with 1932, reduces the item to about $5,000; we have assumed the stipulation speaks the fact, and have dropped it out.

Addition was also made because of payments on account of the 1¾ per cent contract on gas sold to others than the plaintiffs. Part of this expense is justifiable, particularly since the Cities Service Gas Company has no such agreement as the distributing companies have with the Gas Service Company. But the justifiable amount is not proven, and we accordingly add this payment to the operating income of each of the two years.

Depreciation allowance. The Commission found the weighted average per cent for depreciation of physical properties to be 2.96 per cent. This percentage should be applied to the undepreciated values of the physical properties for the reasons set out in State v. Southwestern Bell Tel. Co., 115 Kan. 236, 292; we have treated as depreciable properties those which the parties stipulated as the base for computing engineering and superintendence, $66,425,000. No allowance is made for overheads which the parties agree should go into the rate base undepreciated, for manifestly no annual allowance is necessary for nondepreciable properties. In so doing, we express no opinion as to whether the parties applied correct principles in arriving at their agreement.

Rentals on nonproducing leases. The Company claims a general development expense of $532,530.77, which includes rentals on nonproducing leases, and scouting and geological expense. The latter items enter into the rate base, and there is no proof that such expense will be necessary in the future to increase the already ample reserve supply of gas. Lease rentals are proper, and the Commission allowed rent- [fol. 369] als on 1,060 acres of nonproducing leases. Having determined that the company properly owns a large reserve, the lease rentals must be allowed.

Amortization of nonproducing leases. This point can be best illustrated by an example: Assuming a bonus of $1,000 is paid for a lease not yet producing. We have allowed its value in the rate base, and rentals paid thereon as an expense of operation. When it produces, depletion is allowed. The company amortizes the $1,000 over the life of the lease, presumably about five years, because producing leases are of indeterminate life. If a nonproducing lease, like a motor car, is a depreciable item, the cost should be amortized. But a nonproducing lease is not depreciating, any more than any other real estate, save that it may be

surrendered if found to be nonproductive. When and if it is surrendered, the cost must then be charged to operations or amortized. But should it be amortized before it is developed or surrendered? The question is very doubtful; there is no clear evidence that the 1930 figure of $314,981.68 is apt to be a necessary expense for 1933 and 1934. Accordingly, with hesitation, we disallow the item.

Dry hole expense. The Commission assumed that one dry hole a year would be all that would be suffered in an orderly development of this vast property. The actual expenditure in the test year was $174,747.74, a sum representing the cost of ten or eleven dry holes. The facts must govern. The company is not needlessly drilling dry holes, and geology has not reached the point where only one dry hole a year can reasonably be anticipated by a company owning nearly a million acres of prospective leases, scattered in three states and many fields.

XVII

Under the present rates, the Cities Service Gas Company is earning 7.11 per cent a year upon the present value of its properties.

[fol. 370]

XVIII

A return of approximately 8 per cent upon present values is necessary, under present conditions, to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties. Any return substantially lower than that would be confiscatory. (United Railways v. West, 280 U. S. 234, 252.)

Rate of return. The pipe line company is subject to the hazards attendant upon the production of gas, and its transportation to distant markets. The amount of gas it may take from is own wells; and the price it may charge for its product, is subject to regulation by public authority. It must find a market in a highly competitive field. It competes with coal and fuel oil in household heating and for industrial purposes; the competition of fuel oil is particularly formidable for household heating; improved oil burners are automatic, approved by the National Board of Fire Underwriters for safety, are as clean as gas, and dependable. Electricity has

absorbed the household lighting and is making serious inroads on cooking. In short, it must search for and find its gas; transport it hundreds of miles without an hour's interruption; then find and satisfy its customers. The law contemplates that it make no more than a fair return in good times; it should not be forced to take less, when times are hard. There is evidence that in years past, the profits of the company exceeded 10 per cent. We do not analyze those figures; in rate making, the past must bury its dead; a confiscatory rate cannot be ordered for the future because an exorbitant profit was made in the past. (Georgia Ry. v. R. R. Comm., 262 U. S. 625, 632; Board of Commrs. v. N. Y. Tel. Co., 271 U. S. 23, 32.)

What is a proper return is a question of fact in which the elements of time and place play an important part. In this part of the Middle West, it is a recognized fact that in normal times, public utilities must promise a return of approxi- [fol. 371] mately 8 per cent, if capital for construction and extensions is to be attracted from other investments. The Kansas statutes recognize 8 per cent as a minimum return for waterworks property (sec. 13-1201, R. S. Kan. 1923) and provide for a recapture of a portion of the earnings over 10 per cent of gas and electric companies (sec. 13-1204, id.). The Kansas supreme court has held that earnings from 8 to 9 per cent on telephone properties are reasonable. (The State, ex rel. v. Telephone Co., 115 Kan. 236.) The witness for the Commission testified that 8 per cent would not be an unreasonable return in normal times, but testified that these times are abnormal, as they are. But if abnormality is considered, the return must be increased, not decreased. In these times, when stock of the best utilities can be purchased on a 9 per cent basis or better, certainly an 8 per cent return on this hazardous enterprise is not unreasonable.

## XIX

The order of the Commission would reduce the net revenues of the Cities Service Gas Company by $1,926,145.07. (The amount is stipulated.) Under that order, the return upon the properties dedicated to the public use would be 4.8 per cent, which rate is confiscatory.

XX

If the distributing companies are compelled to pay 40 cents per thousand cubic feet for gas at the city gates, and to base their rates to the consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses, applicable to depreciation and return.

XXI

The distributing companies could not continue their business and pay the Cities Service Gas Company 40 cents per thousand cubic feet, and predicate their rates to the consumers upon 30 cents; the Cities Service Gas Company could not continue its business without the patronage of the distributing companies.

[fol. 372] Conclusions of Law

I

That *portion of the* first order of the commission, made August 31, 1932, that the distributing companies should give no consideration to the payments for gas at the city gates in excess of thirty cents per thousand cubic feet in fixing the rate for the domestic consumer, and the whole of the second order, made August 31, 1932, should be permanently enjoined.

II

The preliminary injunction against the attorney general should be dissolved; its purpose has now been subserved; the permanent injunction will enjoin all officers of the state from undertaking to enforce, directly, or indirectly, the orders herein held void.

III

The costs in this court should be assessed, one-half to plaintiffs and one-half to the defendant Commission.

Orie L. Phillips, Circuit Judge; Geo. T. McDermott, Circuit Judge.

[File endorsement omitted.]

[fol. 373] In United States District Court

Supplemental Memorandum. Filed Jan. 16, 1933

We are advised that a misunderstanding exists among counsel as to the scope of the opinion and findings as to a reasonable return, a misunderstanding doubtless contributed to in part because the court acceded to the suggestion of counsel that findings be made as to all controverted issues, and in part by differing conceptions as to the elasticity of the words "substantially" and "approximately." While supplemental memoranda often confuse instead of clarify, an interpretative resume may not be amiss.

A "reasonable rate" is not a particular decimal. A "reasonable rate" is one that falls within the zone of reason; it is a field, and not a mathematical point. The lower limit of the zone of reason is confiscation, that is, a denial of a net return sufficient to preserve the property and to attract capital necessary to enable the utility to discharge its public duties. A finding that a particular rate is reasonable, is not, therefore, a finding that every other rate is either unreasonable or confiscatory.

With the determination of the proper rate within that zone of reason, the courts are not concerned, for that is a legislative matter. As jurisdiction is invoked here, and generally in such cases, the courts decide but one question: Does the prescribed rate fall below the lower limit of the zone? The rate order in this case allowed a return of 4.8 per cent on the fair value of the property. The issue tendered is the validity of that order. We have held, and hold, that such order is confiscatory. Except in rough approximation, and by way of recital of evidence in the record, we have not undertaken to fix with precision the lower limit of this zone of reason.

Orie L. Phillips, U. S. Circuit Judge. George T. McDermott, U. S. Circuit Judge.

[File endorsement omitted.]

[fol. 374] IN UNITED STATES DISTRICT COURT

DISSENTING OPINION—Filed Jan. 14, 1933

HOPKINS, District Judge, dissenting:

There are suits in equity to enjoin the enforcement of certain orders of the Public Service Commission of Kansas. The questions presented involve the reasonableness of certain contracts between various of the Henry L. Doherty operating corporations.

The facts so far as necessary to this discussion are these:

One of the Doherty Companies, the Cities Service Gas Company, conveys from the gas fields and furnishes gas to the local distributing companies at the various city gates at a contract price of 40 cents per thousand cubic feet. Under another contract each of the distributing companies pays to Henry L. Doherty, doing business as Henry L. Doherty and Co., these items: one and three fourths per cent of its gross revenues, a per diem, an expense charge for certain specific services and an engineering fee of 5 per cent of the cost of construction.

July 2, 1931, the Public Service Commission upon certain findings therein made, entered an order for a hearing to inquire into the reasonableness of such contracts.

The respondents appeared and after a hearing and rehearing the commission, on August 31, 1932, entered an order substantially to the effect "that on and after the 1st day of September, 1932, the distributing companies shall cease to set up on their books as an expense item any payments made to Henry L. Doherty and Co., of the 1¾ per cent charge and also any payments made for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer."

The instant actions were commenced September 19, 1932, to enjoin the enforcement of such order. The bills alleged [fol. 375] diversity of citizenship, that the orders were confiscatory of the property of the plaintiffs, impair the obligation of their contracts, deny to them the equal protection of the law, and unconstitutionally interfere with interstate commerce.

The cases were consolidated for trial. Upon the trial here the same evidence introduced before the commission was received, supplemented by an agreed abstract thereof, an agreed statement of facts and by stipulation and other evidence. These cases are a sequel to Western Distributing Co. v. Commission, decided by this court in 1931, and affirmed by the supreme court February 29, 1932 (285 U. S. 119).

At the threshold of this inquiry we are met by six propositions which must be kept in mind throughout the investigation:

1st. Natural gas is one of the great natural resources. It is discovered, extracted from the earth, transported and sold to the people of a hundred and twenty-eight cities and towns involved in this inquiry. The respondent has secured control of this great resource for which the people must now pay.

2d. That while the problem in this territory a few years ago was one of finding gas to supply the demand, it is now a question of finding a market for what appears to be an almost inexhaustible supply.

3d. That the Henry L. Doherty organization is perhaps one of the most efficient ever known, engaged in the handling of public utilities and products thereof, for which reason it has good credit and is enabled to borrow necessary funds for its operations at the lowest available rates.

4th. That within the past two and a half or three years utility rates in this territory have perceptibly fallen and that a return of from five to seven per cent is now equal to the purchasing power of from seven to ten per cent during the period of prosperity just preceding that time.

[fol. 376] 5th. That it is a matter of common knowledge that the Doherty organization has been and is selling and offering to sell gas to individual consumers in this territory, not only for industrial, but for domestic purposes, at rates far below the thirty-cent rate fixed by the public service commission to the distributing companies at the city gates.

6th. That while public utility rates in general throughout this territory have been perceptibly lowered during the last two or three years, the Doherty forty-cent rate at the city gates, has remained the same.

The commission contends that the order under inquiry is not subject to the constitutional objections urged by the

plaintiffs because it finds only that the contracts are unreasonable and that the extent of such unreasonableness. I do not agree with this contention. The order expressly prohibits payments made to Henry L. Doherty & Co., and to the Cities Service Gas Co., for gas at the city gates in excess of the thirty cents per thousand cubic feet "in fixing a rate for the domestic consumer," on and after September 1, 1932. The order, in my opinion, would affect the rates charged the domestic consumers and is in fact a rate-reducing order, and is therefore subject to review.

There is no contention on the part of the Commission that it has power to regulate interstate gas rates. However a state does have the power to regulate the price of gas brought into it and sold directly to the consumer, because "the business of supplying local consumers is a local business, even though the gas be brought from another state" (Missouri v. Kansas Gas Co., 265 U. D. 298, 309; Penna. Gas Co. v. Public Service Comm., 252 U. E. 23; East Ohio Gas Co. v. Tax Commission, 383 U. S. 465).

In spite of a stipulation between the parties, I do not concur in the view that if the charge made by the plaintiff at the city gates was reduced to thirty cents it would result [fol. 377] in a reduction of $1,926,000 in its net income. In all human probability a reduction in rates would induce a greater demand for gas. The plaintiff states that other fuel costs have been reduced. For instance, at page 104 of its brief it says:

"In 1924 and 1925 many of these distributing companies were acquired by the Cities Service organization and at no time from then until now has there been any failure in service. Natural gas in this territory does not have as many outages as does electric service which is always taken as the ideal service in the utility field at which to aim. The best evidence in this improvement in service is shown by the annual reports to the Public Service Commission which show the *increased annual sales of gas per customer in all of the towns in this territory throughout the last six or seven years, notwithstanding the fact that during this period the cost of competitive fuels was steadily being reduced, coal and oil now selling at prices hitherto unknown.*"

At page 106 it says (on the question of interest rates):

"No changes in gas rates from 1922 to date have been made except reductions. These distributing companies have not yet recovered from the effects of their experience as isolated companies to an extent whereby they are able to furnish their own financing for extensions and betterments at a reasonable cost. But they have at all times been furnished with whatever money was needed for additions and betterments by the Cities Service Company and they have been charged an *interest rate of only 6 per cent for this money.*"

But the 40 cent gas rate has not been reduced. Nor do I concur that a rate of 8 per cent upon present values of the plaintiff is necessary under present conditions to secure confidence in its financial soundness, or to maintain its credit and enable it to borrow money.

I do not assent to the conclusion that forty cents per thousand cubic feet at the city gates is a reasonable charge and that to compel the plaintiff to furnish such gas at thirty cents per M. C. F. will result in confiscation of its property.

I concur in the view of the majority that the various [fol. 378] Doherty companies are engaged in a common enterprise and that the principal one, the Cities Service Company, is through the agencies of the other corporations, supplying gas to the local consumers and is therefore engaged in a local business. The fact is that the Henry L. Doherty organization is one of the most efficient, far reaching monopolies operating in this country. It has many interlocking corporations. The common stock of the Cities Service Gas Company is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. Henry L. Doherty & Co. is Henry L. Doherty, who owns 35 per cent of the voting stock of the Cities Service Company and controls its policies. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the Cities Service Gas Co. Henry L. Doherty in fact controls the policies of all the interlocking companies.

Since as far back as 1910 Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has been completing and building up this organization. It is

manned by experienced executives, financial advisors, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technical experts, accountants, operators and lawyers. All are men high in their various professions. Through the years they have learned the Doherty way. They see through the eyes of Mr. Doherty, understand the Doherty language, ("their master's voice,") and speak the voice of Mr. Doherty. This is not said in criticism of the Doherty organization, nor of the men high in their professions and avocations, who manage and direct it, but only to illustrate this efficient, powerful, operating machine known as the Doherty organization. With due credit to the poet Pope, it may be observed:

"That all are parts of one stupendous whole,
Whose body many corporations are, and Doherty the soul."

I also concur in the view that since the Doherty compa- [Fol. 379] nies exercise a monopoly for supplying gas to the various communities served by the distributing companies, parties herein, and since the Cities Service Gas Co., is the unit which procures, conveys and delivers the gas to the other companies, that the only method of determining the fairness and reasonableness of the charge at the city gates is to determine the reasonableness of the return to the Cities Service Gas Co., on its property used and useful in such business.

I further concur in the view That in determining the facts, the findings of the Public Service Commission are presumed to be correct (Blanton v. Belt Line Ry. Corp., 268 U. S. 413, 422; Cotton v. Kansas City Stockyards Co., 183 U. S. 79; Denver Union Stockyard Co. v. United States [D. C. Colo.] 57 Fed. 2d 735, 739), and that, on the question of confiscation, the plaintiff is entitled to the independent judgment of a judicial tribunal as to the law and facts. (United Railways & E. Co. v. West, 280 U. S. 234, 251; Blue Field W. W. & Imp. Co. v. Public Service Commission, 262 U. S. 679, 689; Ohio Valley W. Co. v. Ben Avon Borough, 253 U. S. 287; Lincoln Gas Co. v. Lincoln, 223 U. S. 349; Crowell v. Benson, 285 U. S. 2269.)

A contention that the commission is not concerned with the future is not well founded. It is settled that the Commission is concerned with rate for the future, and the ex-

perience of the past is the only criterion by which it may make rates for the future.

The history of this company shows rapid development since 1926, when taken over by Mr. Doherty, as to investment in plant increase, in sales of gas and in net income. For instance, gas sales in 1927 amounted to $10,771,491; in 1930 $15,380,609, an increase of 42.79 per cent. Investment in plant increased from December, 1927, to December, 1932, 50.23 per cent. During the same period net earnings increased 65.48 per cent. During this period what is known as the Amarillo Wichita Ottawa line was completed, and extensions were made of major importance to Nebraska [fol. 380] and Missouri, developing new markets for the business. In 1930 the effect of the depression began to affect sales and earnings of the company largely through loss of industrial business, a business bound to be regained as industrial business improves; and it goes without saying that the carrying of the investment and expense of industrial business should not be placed on the domestic consumers.

Sale of gas for drilling and field purposes during 1932 period were only 36.55 per cent of such sales during 1930 (showing abnormality during 1932) and it is reasonable to expect that with the return of activity in the oil and gas business the markets for drilling and field gas will be revived.

Earnings should be averaged over a reasonable period of time in order to determine whether a utility is earning a fair return, or more or less than a fair return, for rate making or any other purposes. (Denver Union Stock Yards case, supra.) "The only fair test is to level out the peaks and valleys and estimate the future according to the mean line." Complaint is made that the commission used an average value. The same reasoning which requires the use of average earnings requires the use of average values. It is not fair to compare earnings during 1929 and 1930, with the values in 1931 and 1932, when there were extensive additions to plant investment. The use of average values contemplates the inclusion of values averaged over the same period used for the averaging of earnings.

In connection with the specific questions raised are general questions of public policy. This organization has secured control of a great natural resource for which the people must pay. The question for determination is what

charge constitutes the rate base for this plaintiff in arriving at a fair value of its property and what would be a reasonable rate to charge for the product and services rendered to the people. How shall the people of these hundred and twenty eight cities and towns be permitted to enjoy this natural resource free from extortion and at the same time allow the utility a fair return on the value of its property? [fol. 381] The showing must be clear before the court should interfere with the commission's order. Especially is this true where no actual experience has been had of the practical result of the rates fixed. While there is an alleged prophesied loss of income from a reduced rate, it must not be overlooked that such reduction means probably increased consumption.

In Wilcox v. Consolidated Gas Co., 212 U. S. 41, it was said:

"Where the rate complained of shows in any event a very narrow line of division between possible confiscation and proper regulation as based upon the value of the property found by the court below, and the division depends upon opinions as to the value, which differ considerably among the witnesses, and also upon the results in the future of operation under the rate objected to, so that the material fact of value is left in much doubt, a court of equity ought not to interfere by injunction before a fair trial has been made of continuing the business under that rate, and thus eliminating, as far as is possible, the doubt arising from opinions as opposed in facts."

. . . . . .

"There is no particular rate of compensation which must in all cases and in all parts of the country be regarded as sufficient for capital invested in business enterprises. Such compensation must depend greatly upon circumstances and locality among other things, the amount of risk in the business is a most important factor, as well as the locality where the business is conducted and the rate expected and usually realized thereupon investments of a somewhat similar nature with regard to the risk attending them."

F. C. Hamilton and E. B. Black were the principal engineers testifying in this case. Both are eminent in their profession. Mr. Hamilton for many years a member of

the Doherty organization learned in that organization's activities, knowing its business, being interested therein, naturally an efficient and proficient booster of its values when rate matters are involved. All this may be said without in any manner impugning the ability or high character of Mr. Hamilton. It only directs attention to the fact that he has been for many years and is interested in the success of the Doherty organization. That his education and environment have all developed a viewpoint [fol. 382] which necessarily is for the benefit of the utility. That he is an interested witness.

Mr. Black is an independent engineer, a member of the old firm of Worley & Black, now Black & Veatch, of high standing and operating for many years, secured by the state for the purposes of this case.

The Commission saw and heard the witnesses, painstakingly examined their testimony and with the discretion allowed it under the law, arrived at what it determined the fair and reasonable value of plaintiff's property. And while it is the duty of this court to make an independent investigation of the facts which it has done, this court should be careful not to substitute its judgment for that of the Commission, unless it is clear that the Commission erred.

The effect of the opinion and findings of the majority, if adopted on sufficient of the items, makes a rate base from which it may be argued that the rate allowed the plaintiff is confiscatory. The evidence in my opinion fails to disclose on such items sufficient reasons for setting aside the findings of the commission and substituting those of this court, nor does the evidence justify a finding of this court that a gate rate of 40 cents to the distributing companies is fair and reasonable.

The important questions will be discussed in their order.

## Used and Useful Gas Acreage

The company owns 1,262,361 acres of gas rights. The Commission found that 71,267 of such leases were used and useful and devoted to a public use, and valued such acreage at $2,880,390. (Book value.)

Officers of the company testified that they considered all of the 1,262,361 acres of gas rights owned by the com-

pany as necessary and a prudent purchase. The majority opinion holds that the public service commission may not substitute its judgment for that of the officers of the companies. True ordinarily, but the rule also is that "what [fol. 383] the company is entitled to demand in order that it may have just compensation, is a fair return upon the reasonable value of the property at the time it is being used for the public." (Pon on Public Utilities, sec 591; San Diego Land & Town Co. v. National City, 174 U. S. 739; 43 L. Ed. 1154.)

The facts show clearly, in my opinion, that all of such gas rights are not now used, and that the present consumers do not and will not in the near future receive any benefit from them.

These investments in gas reserves, by the plaintiff, perhaps were prudent, but they should not be used as a base on which to estimate the rate for present consumers. None but the 71,267 acres of leases allowed by the commission are in my opinion used and useful and devoted to the public use.

This 71,267 acres comprises 50,000 acres proven in the Amarillo field with all the wells in that field, and 21,261 acres, all the developed, proven and probable acreage in Kansas, Oklahoma (except Hugoton); with all the wells in those fields the recoverable gas reserve in this 71,267 acres is sufficient to furnish all of the company's requirements, excluding the gas purchased under its purchase contracts, on the basis of its requirements for the year 1930, for twenty-two years.

The acreage in the Hugoton field excluded comprises 123,440 acres. None of the company's acreage in this field is drilled, and all of it is distant at least ninety miles from any pipe line owned by the company. It is held by the company through ten-year leases with about seven years yet to run. These leases require an annual rental be paid and that a well be drilled within the term of the lease. The number of these leases is in excess of 500. The cost of drilling and equipping a well in this field is not less than $20,000, and if the company is to hold these leases it must drill within the next seven years over 500 wells at a cost of over $10,000,000 and in addition pay annual rental in a substantial amount.

[fol. 384] The prospective acreage excluded by the commission amounts to 998,287 acres; it is "wildcat" terri-

tory. Its value is for oil rather than gas. It is scattered. Very little of it is available to the company's pipe line.

In the assignment of 71,267 acres of leases as used and useful, there are 27,910 acres of land in the Sweet proven area of the Amarillo field, which are not developed, and 1,385 acres in Kansas and Oklahoma, 325 acres of which are proven and 1,060 acres probable, which are yet to be drilled, with sufficient reserves of recoverable gas to last for twenty two years. In addition to this reserve, the company owns purchase contracts entitling it to the gas of 782,421 acres in Kansas and Oklahoma, having 1,502 wells and a daily open flow of 2,138,170 M. C. F.

Gas consumers should not be required to pay a rate for gas based on a return on the valuation of leases which are not used for them, and which if ever used will not be until the distant future.

The gas situation, in this territory, has undergone a complete change within the last five years. The Amarillo and Hugoton fields have been developed within that time. Prior to that time the problem was how and where to get gas. Now the problem is to find a market. Utilities then based their rates on the presumption that the gas supply would be exhausted in from seven to ten years. Now the supply appears almost inexhaustible.

Doctor Moore, state geologist of Kansas, testified that the recoverable gas in the Hugoton field alone is sufficient to supply all of the requirements of Kansas, domestic and industrial, at the present rate of consumption, for over one hundred years.

It is a matter of common knowledge that there was recently brought in the "Burton" field within three miles of this company's pipe line, with undefined limits, having wells with an open flow of 270,000,000 cubic feet per day, with a rock pressure of 1,200 pounds.

Another matter having a bearing on this controversy is [fol. 385] the problem confronting the Texas railroad commission in the Amarillo field as to means of providing a market for the vast amount of "shut in gas"; that is, gas wells which have been drilled by independent operators which are shut in for lack of market.

The first attempt to provide a market for this shut in gas was by the common-purchaser act, which required purchase of this gas by the gas companies. That act was de-

clared unconstitutional, whereupon the Texas commission recently made an order limiting the "take" to 4 per cent of the potential (open flow). The object of this order appears to be two fold, first to conserve the gas in the sweet proven area in the Amarillo field for domestic and industrial uses; second, to provide a market for this shut in gas and a ratable taking from all wells. This order is in litigation. Whether or not it may be sustained makes little difference to this plaintiff. It may purchase gas from the shut in wells, many of which are within two miles of its line, or it may develop its own acreage (50,000 acres) by drilling additional wells.

That is to say, the effect of the Texas order, if sustained, is not to require the company to have additional acreage, but to require additional wells on the acreage which has been allotted to it; or the company if it prefers, can dispense with its reserves and in lieu thereof purchase some of the vast quantity of gas available from the "shut in wells," which under present conditions can find no market.

The action of the Kansas Commission in including in the rate base only that acreage which presently and will in the near future be used and useful is well supported by the authorities. (See United Fuel Gas Company v. Public Service Commission, 73 Law E. [U. S.] P. 402, 78 U. S. P. 322; United Fuel & Gas Co. v. Public Service Commission of West Virginia, 178 U. S. 722, 73 Law Ed. [U. S.] 402; City of Erie v. Public Service Commission, 278 P. A. 512; 123 Atl. P. U. R. 1924 D. 89; Logan Gas Company v. Public [fol. 386] Utilities Commission of Ohio, 189 N. E. 575; Columbus Gas and Fuel Company, No. 5925, supra.)

In my opinion the Commission was well within its powers in finding that 71,267 acres of plaintiffs' gas reserves, which are in addition to its purchase contracts, covering 782,421 acres and 1,502 wells, with a potential of 1,532,625 M. C. F. per day, are used and useful to the company's developed acreage 27,910 acres of which is in the sweet proven gas area of the Amarillo field. The testimony of the officers of the company that they considered all of the 1,262,261 acres held by it as necessary for its future requirements, is not sufficient to overcome the actual facts, that it has an adequate supply for twenty-two years in the future. It would be contrary to common sense and justice to require the present consumers to pay for gas reserves which are not now used and which might never be used for their needs.

The facts and circumstances disclosed by the record in this case present a problem different from the ordinary rate case. We have here a producing gas pipe line built for the purpose of supplying already existing customers. Result:—going-concern value is very largely opinion based upon theory, when the theory is not supported by the facts.

Mr. Black, testifying for the Commission, found the going value to be $3,820,000. Mr. Hamilton, engineer for the Doherty Corporations, found it to be 8,898,532. The Commission found $2,000,000 as a sufficient allowance for this element of value. Mr. Hamilton testified: "I just took 10 per cent of the physical property value for this particular case for that item."

"Q. You have not itemized it?

"A. No, I have not itemized it in any way.

"Q. As I understand, then you did not arrive at it by finding the cost of attaching this business.

[fol. 387] "A. It is partially the cost of attaching the business, and the time of the engineers and others in negotiating the contracts, but that, for a wholesale situation, is a small item. The largest cost is the excess capacity that you will have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on."

It is apparent from the record that Mr. Hamilton and Mr. Black considered the "idle plant" while the line was reaching the maximum capacity as the largest element of cost to be considered in going-concern value.

Both witnesses testified that the going-concern value for a pipe-line company would be less than the going value for a distributing plant. Mr. Hamilton testified to the difference between going value for a distributing plant and a pipe-line company as follows:

"Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

"A. No, because there would be a different allowance between your pipe-line plant or your distribution plant or an electric plant or something like that. There might be a wholly different basis.

"Q. For instance you take the distribution plant, take the one here in Topeka, for example——

"A. Yes, sir.

"Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

"A. That is true, and 10 per cent allowance in that distribution plant would not be sufficient in my judgment.

"Q. Then take a pipe-line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

"A. That is true.

"Q. That should be taken into consideration in arriving at the going value in this case?

"A. That is true."

It is perfectly apparent that both witnesses arrived at their calculations for idle plant upon a hypothetical basis without considering the actual facts and experiences of the company. It appears that the Commission applied the tests [fol. 388] which both engineers laid down as a proper measure of determining going-concern value and found that $2,000,000 was a sufficient and proper allowance.

The record shows clearly that on the major part of the pipe-line system there was very little idle plant following the construction period.

Many reasons may be advanced as to why a going-concern value should be added to the physical value of the property of the distributing companies which does not obtain as to the production and transmission system. This line was built for the definite purpose of supplying customers already secured and there appears little or no justification for adding a large going-concern value to it.

It is doubtful if a going-concern value amounting to millions of dollars can be established on a theory that expenses are to be incurred after the property has been reproduced when as a matter of fact such expenses were not incurred. How can it be said that there would be any expense of attaching business to a producing pipe-line company which has been built for the sole purpose of supplying already existing customers?

The argument that the cost incident to training personnel is a proper basis of going-concern value in this case is not

good, because the business of producing, transporting and distributing gas has been so long in operation that an abundant supply of well-trained personnel is always at the command of the company. In these times there is probably a considerable oversupply. See (in re appeal Columbus Gas and Fuel Co., [Ohio], No. 5935.)

The Commission, in my opinion, was right when it gave consideration to the cost of organizing the operating company, organization legal expenses, cost of records, and some interest and depreciation on idle plant, taking into consideration that there has been very little, if any, idle plant in the system.

It may be observed in passing that the interest charged [fol. 389] on the books of the company to the cost of Wichita Ottawa 20 inch line amounted to $24,444.04, while Mr. Black allowed for interest on this same line $198,544, and Mr. Hamilton allowed $320,182, indicating that both engineers were not only liberal, but, in fact, made excessive allowances for interest compared with the actual experience of the company. Under all the circumstances the allowance of $2,000,000 made by the commission was reasonable and adequate.

## Rate of Return

In considering what is a fair rate of return to be earned by the pipe line company in connection with the reasonableness of the gate rate contract of 40 cents, we must take into consideration what it must earn in the light of its situation, its requirements and its opportunities. In dealing with its affiliated distributing companies we should consider the fact that the company should be allowed to earn on the value of its property employed in serving the public with its pipe line an amount equal to that generally being made by the same business undertakings which are attached by the same risks and uncertainties. It should also be allowed to earn an amount reasonably sufficient to assure confidence in its financial ability.

There was testimony for the plaintiff that an 8 per cent return is usual. Other testimony placed the rate at from 6 to 8 per cent. Practically all of the witnesses agreed that some consideration should be given to the fact that this company was not an ordinary public utility company, but one of a large system organized for the purpose of main-

taining the credit of the constituent companies and securing financial assistance.

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It is apparent from the affiliation and mutual assistance rendered by the great and efficient Doherty organization that this particular plaintiff is and has been able to sell its securities at an "interest rate that was from a half to three fourths per cent less than anything else that was put out [fol. 390] at about that time on a similar project, and that if gets better terms on its mortgages. Because of this situation it was able to sell its 5½ per cent bonds for 96¼. This plaintiff having ample resources does not necessarily have to issue securities now or six months from now or two years from now. "It picks and chooses its time when the markets are right."

The record shows this plaintiff sold twelve million dollars of first mortgage, pipe line 6 per cent gold bonds at par. It is apparent therefore that it is able to obtain funds at a very low rate and is assured of financial stability and a supported credit which enables it to raise all necessary money for the proper discharge of its duties at a low rate of interest. It is apparent also that there is little risk or hazard in its business. The pipe line system which it has established is a permanent fixture for an indefinite period. It has a gas reserve which insures it of a supply of gas lasting well into the future. The territory which it serves is well protected; it has almost a monopoly on the territory which it serves due to the fact that the distributing units are affiliated companies and it would be economically unsound for another pipe line company to invade its territory.

We are also confronted with changed conditions affecting opportunities for investments which tend to limit the amount of the return. Annual returns upon capital have materially decreased in the past two or three years. Businesses generally are satisfied with a very low rate of return. All businesses, including that of public utilities, are satisfied with a much less rate of return than they were three or four years ago when annual returns upon the capital were unreasonably high.

The Cities Service Gas Company is not an ordinary public utility. It is one of a large system organized for the purpose of maintaining the credit of subsidiary companies and

assisting them in their finances. It has been able to extend its business so as to meet increased demands, to pay its [fol. 391] operating expenses, including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and accumulate a large surplus. (See Smith v. Illinois Bell Telephone Co., 282 U. S. 159, 161.)

It is apparent from the record that the operations of this plaintiff have been highly successful and enormously profitable. It was organized in 1926, acquiring the assets and assuming liabilities of the following companies: Empire Natural Gas Company, Empire Gas and Pipe Line Company, Kansas Oklahoma Gas Company, Empire Gas and Fuel Company (gas properties only).

At that time the plant investment of these companies, including uncompleted job orders, was $52,182,525.98. Reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95, or 42.97 per cent of the plant investment. They had accumulated a surplus amounting to $14,903,660.21, equal to 87.26 per cent of the total capital stock of the companies taken over.

The combined reserves for depreciation and depletion and surplus amounted to $37,327,527.16, equal to 218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment. They were able to loan other affiliated companies $7,559,571 in addition to paying bond interest and dividends.

When this plaintiff was organized and its books opened, 17,080,000 of capital stock and $2,000,000 of bonds became immediately $25,000,000 of common stock and $25,000,000 of 5½ per cent bonds; its reserves for depreciation and depletion became $7,760,706 instead of $22,423,939, as they were before the consolidation. No surplus was carried over into the new corporation.

A glance at the financial history of the company since the consolidation in 1926, is of more than passing interest. This history shows that surplus has been accumulated in excess of all interest and dividends paid of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have [fol. 392] been increased to $10,818,020. Its total assets have increased from $60,595,001 as of December, 1926, to $109,431,039 as of June 30, 1931. This increase was accomplished with the addition of the outstanding stock and bonds

of only $28,305,700 and loans of $9,000,000. The company has been able to advance to affiliated companies $2,677,131. During all this time it paid interest on its bonds and dividends on its capital stock; in 1928, $1,000,000 dividends, and in 1929 and 1930, $2,000,000 each on dividends, which is at the rate of 8 per cent per annum. Its earnings before interest were as follows:

| | | | |
|---|---|---|---|
| 1927 | $5,335,739 | 1930 | $3,829,480 |
| 1928 | $6,053,621 | Twelve months ending | |
| 1929 | $8,060,793 | June 30, 1931 | $3,741,966 |

Its net profit after paying all interest and other charges providing for substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

| | | | |
|---|---|---|---|
| 1927 | 9.96% | 1929 | 14.53% |
| 1928 | 6.75% | 1930 | 10.82% |

The plant investment, including uncompleted job orders, increased from $54,243,128, December 31, 1926, to $99,003,998, June 30, 1931, an increase of $45,760,872. A considerable program of expansion was carried out, a large line was constructed from Amarillo to Wichita; a line was extended from near Hutchinson north into Nebraska; lines were extended into Missouri; such construction involved large expenditures which affected the operating expenses of the company.

It is a matter of common knowledge that price levels were higher. The purchasing power of the dollar was very much less than now, 8 per cent was considered a fair and reasonable rate of return.

Under the present low level of prices the purchasing power of a return of 6 per cent is greater than the purchasing power of a return of 8 per cent was during the periods of higher price levels.

[fol. 393] A return of 6 per cent is not unreasonable at this time. In fact, the great majority of concerns now doing business are glad to earn as much as 6 per cent, and are fortunate to do so. Even a 5 per cent return at this time would not be confiscatory.

I am of the opinion that in view of the financial history of this plaintiff its highly profitable experience, the fact that it is a part of a large system with its market assured through affiliated distributing companies, its large gas reserves, and all attending circumstances, a return of 6 to 8 per cent is reasonable and 5 per cent would not be confiscatory.

United Railways & Electric Co. v. West, 280 U. S. 234-291, 74 L. Ed. 390, is cited and relied on in the majority opinion as sustaining the conclusion that the rate of return must be 8 per cent. The court in the West case held that under the circumstances of that case a rate of 6.26 per cent was insufficient. Three members of the court dissented. In my opinion the decision in the West case does not sustain the majority opinion in this case. It was among other things said in the syllabus:

"* * * The fair rate of return to which a public utility is entitled is to be tested primarily by present-day conditions, and not by what may have been a proper rate in the past. * * * In determining whether the rates established by a public service commission are so inadequate as to be confiscatory, the court must determine what will constitute a fair return, to the best of its ability, in the exercise of a fair, enlightened, and independent judgment as to both law and facts. * * * A rate producing a return of 6.26 per cent on the valuation of the property of a street railway company will be considered so inadequate as to amount to a taking of its property without due process, where it is shown that while the total number of passengers carried has for some time steadily decreased, the number carried during rush hours has increased, resulting in an increase of expenses in proportion to the whole number of passengers carried and that, in borrowing money with which to finance its operations, the company has been obliged to pay a rate of interest ranging well over 7 per cent."

[fol. 394] In the opinion it was said (p. 250):

"A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same gen-

eral part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally. * * * Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest in such an undertaking. Low, uncertain or irregular income makes for low prices for the securities of the utility and higher rates of interest to be demanded by investors. The fact that the company may not insist as a matter of constitutional right that past losses be made up by rates to be applied in the present and future tends to weaken credit, and the fact that the utility is protected against being compelled (p. 251) to serve for confiscatory rates tends to support it. In this case the record shows that the rate of return has been low through a long period up to the time of the inquiry by the Commission here involved."

On page 251 appears the following:

"Since 1920 the company has borrowed from time to time some $18,000,000 upon which it has been obliged to pay an average rate of interest ranging well over 7 per cent and this has been, upon the valuation fixed, with an allowance for depreciation calculated with reference to that valuation, and upon the then prescribed rates, the company for the years 1920 to 1926, both inclusive, obtained a return of little more than 5 per cent per annum."

On page 252 appears the following:

"In this view of the matter, a return of 6.25 per cent is clearly inadequate. In the light of the recent decisions of this court and other federal decisions, it is not certain that rates securing a return of 7½ per cent or even 8 per cent on the value of the property would not be necessary to avoid confiscation. But this we need not decide, since the company itself sought from the commission a rate which

it appears would produce a return of about 7.44 per cent, at the same time insisting that such return fall short of being adequate.

[fol. 395] On page 249 appears the following:

"What is a fair return within this principle cannot be settled by invoking decisions of this court made years ago based upon conditions radically different from those which prevail today. The problem is one to be tested primarily by present day conditions. Annual returns upon capital and enterprise, like wages of employees, cost of maintenance and related expenses, have materially increased the country over. This is common knowledge. A rate of return upon capital invested in street railway lines and other public utilities which might have been proper a few years ago no longer furnishes a safe criterion either for the present or the future."

The court was there considering a rate for a street railway. It is a matter of common knowledge to which we may not shut our eyes, that bus transportation and the use of private automobiles the country over have cut deeply into the revenues of street railway companies. The very opposite condition exists in connection with the plaintiff which has made big returns, paid its interest and dividends, accumulated a surplus, loaned money, and is able to float its securities at will and on better terms than other like utilities. A gas pipe-line company which practically has a monopoly in its field.

Applying to the instant case the principles stated by Mr. Justice Southerland in United Railways v. West, supra: Considering all the facts shown by the record and attending circumstances, it must appear beyond question that a rate of return to the plaintiff of from 6 to 8 per cent on the value of its property used and useful in its business would be a fair return when protected by the state—even a rate of 5 per cent in these times would not be confiscatory.

In Wabash Valley Electric Co. v. Ralph M. Young et al., No. 112, a case in which a decision was handed down January 9, 1933, in an opinion by Mr. Justice Southerland it was said:

"It is true, as appellant point out, that in United Railways v. West, 280 U. S. 234, 251-252, this court held that a rate of return for a street railway of less than 7.44 per cent was confiscatory, saying that sound business manage- [fol. 326] ment required that after paying all expenses of operation, etc., 'there should still remain something to be passed to the surplus account,' and that a rate of return which did not admit of that being done was not sufficient to enable a utility to maintain its credit and raise money for the proper discharge of its public duties. Many cases were cited tending to show that a return of 7½ per cent, or even 8 per cent, might be necessary, but it was said (pp. 249-250) that no rule could be laid down which would apply uniformly to all sorts of utilities. 'What may be a fair return for one may be inadequate for another, depending upon circumstances, locality and risk.' A street railway company, compelled to meet the growing competition of private automobiles, public omnibuses, and other motor carriers, well might sustain such losses of revenue because of the decreased number of passengers carried, as to require a larger rate of return than would be required by an electric company like appellant, which not only enjoys a practical monopoly in the field where its services are rendered, but whose financial structure, it fairly may be assumed, is greatly strengthened by its affiliations and by the interested support of the parent company to which it belongs. On the whole we are unable to conclude that a 7 per cent rate of return, under the facts here disclosed, is so low as to be confiscatory. See Smith v. Illinois Bell Tel. Co., supra, at pp. 160-161."

In Kankakee Water Co. v. Gilbert, decided by the United States district court for the eastern district of Illinois January 6, 1933, it was said that "under existing depressed, industrial and financial conditions a rate of 5.17 per cent was not confiscatory." The court said:

"Under the existing generally depressed industrial and financial conditions, indicating a greatly abnormal condition both generally and locally, all of which appears in the record, we are not warranted in finding that the probable return of 5.17 per cent upon the valuation as aforesaid, furnished by the commission's prescribed rates, is con-

fiscatory. In this connection, we have considered the evidence of present return in industrial enterprises of other character, and that of similar utility companies, as well as the fact that plaintiff makes no claim and furnishes no evidence that new capital is at present needed in its business."

[fol. 397] The Henry L. Doherty Contract

The distributing companies pay to Henry L. Doherty 1¾ per cent of their gross revenue, an engineering fee equal to 5 per cent of construction, and in addition expenses, disbursements and per diem for Henry L. Doherty & Company representatives while at the property of the distributing companies or traveling for them on special matters.

The distributing companies also pay to the Gas Service Company for the same type of service. The commission allowed payment for the services to the Gas Service Company, but refused approval or payment to the Henry L. Doherty & Company on the ground that it was a duplication.

What happens is perfectly clear. The distributing companies have similar contracts with two of these other Doherty units for the same class or type of service—one with Henry L. Doherty, the other with the Gas Service Company. The latter furnished the services, the former did not.

The Public Service Commission made an allowance for the services by the Gas Service Co., but denied any allowance to Henry L. Doherty & Co. The majority opinion, while denying payment to Henry L. Doherty & Company because of failure of proof that services were rendered, holds that the contract is proper. With this I cannot agree.

Application of the rule that a public utility is entitled to charge such rates as will create a sufficient income to provide a fair return upon the value of its property used and useful and devoted to the public, does not authorize the owners of a utility to pay themselves increased operating expenses or to provide themselves with unconscionable profit because of their position. Funds for operating expenses are received from the public and to thus duplicate payments for services is unwarranted under any reasonable hypothesis.

[fol. 398] The record shows that the activities of Henry L. Doherty and Company embrace many matters which, by the greatest stretch of the imagination, could not be a proper operating charge to the distributing companies. These activities are largely devoted to the purchase and sale of Cities Service securities. Investments of the Cities Service Company and Henry L. Doherty & Company in oil development and others in no way results in a benefit to the distributing companies. It appears that no securities of the disfributing companies have been marketed by Henry L. Doherty and Company, and should there be, a separate fee would be charged for such services. The production, sale and transportation of oil and the handling of New York real estate are activities unrelated to the distributing companies and the consumers of natural gas have no interest in Mr. Doherty's oil or stock business and should not be compelled to pay the expense of transacting such business. There is no apparent reason why the patrons of these distributing companies should pay to help maintain an office in London. Yet for a period of years the distributing companies have been paying Henry L. Doherty & Company 1¾ per cent of their gross revenue from funds received from their patrons.

A number of companies are operated by Henry L. Doherty & Company at 60 Wall Street, which in no way, so far as the record discloses, contribute to the defraying of the expense of the operation of Henry L. Doherty & Company.

For example: The Gas Securities Company owned by Henry L. Doherty & Company, with offices at 60 Wall Street, with net assets of $23,252,907 and net earnings for 1929 amounting to $1,960,376, was not shown to have paid any revenue to Henry L. Doherty & Company.

The Gas and Electric Securities Company owned and operated by Henry L. Doherty & Company, with offices at [fol. 399] 60 Wall Street, has assets of $24,952,188, with an income of $2,086,069 in 1929, with no showing of revenue to Henry L. Doherty & Company.

This Henry L. Doherty contract apparently is for the purpose of keeping Henry L. Doherty informed as to the activities of the distributing companies and the protection of his investment rather than for the benefit of the distributing and pipe-line companies. Except to the extent

that any specific services may be rendered, there is nothing in the record to show any benefits to the distributing companies from his contract. The benefit is largely for the sole benefit of Mr. Doherty's holding company, The Cities Service Company.

The activities of Henry L. Doherty & Company may well be considered a burden to the distributing and pipe-line companies, rather than a benefit. First, because they must immediately transfer all their earnings to Henry L. Doherty & Company, leaving them dependent upon it for financial existence for which they must pay, while Henry L. Doherty & Company has the advantage of these earnings and the use of the funds of the underlying companies pending their distribution as dividends; and second, because they must pay Henry L. Doherty & Company 5 per cent of the cost of their construction projects, regardless of the benefit received or the services performed. While this cannot enter into the expense in determining a rate to be charged the consumer, it does affect the financial stability of the distributing and pipe-line companies.

Not only did the parties fail to produce any evidence to sustain their rights to such fee, as stated in the majority opinion, but they failed in my opinion to justify the need of such a contract.

## Interest During Construction

Black and Hamilton both calculated interest during construction for the same period. Black allowed a rate of 6 per cent, Hamilton 8 per cent. The question is, what is a proper rate?

The plaintiff argues that "if 8 per cent is a proper rate of [fol. 400] return for the investor to receive after the project is placed in operation, on what theory or by what process of reasoning can the conclusion be reached that this same investor is entitled to less return on his money during the period the plant is being constructed? You have the same investor and the same money going into the same project. Whatever is fair in one case must be fair in the other."

With this contention I do not agree. There is little relation to be found between a rate of interest to be allowed for the use of money borrowed or advanced in construction

and a rate of return on the value of property when subsequently put into public service. The latter involves the contingencies of operation and many other considerations.

Interest during construction may be a different rate. It is a fixed allowance and the hazards which may accompany the earning of a rate after the business is in operation are not present.

The allowance by Black as heretofore said was not only adequate, but excessive. Hamilton's allowance was entirely out of line with the actual facts.

On September 1, 1931, there were properties of the City Service Gas Co. used and useful in the public service, as follows:

| | Number and title of account | Reproduction cost less depreciation |
|---|---|---|
| 1307 | Production—rights of way | $55,982 |
| 1310 | Production—field measuring, station structures | 35,909 |
| 1311 | Production other structures | 47,876 |
| 1312 | Production gas-well construction | 1,294,710 |
| 1313 | Production gas-well equipment | 658,439 |
| 1314 | Production field-line equipment | 3,126,159 |
| 1315 | Production field measuring station equipment | 265,746 |
| 1316 | Production drilling and cleaning equipment | 27,908 |
| 1317 | Production other equipment | 1,333 |
| 1325 | Transmission land | 145,202 |
| 1327 | Transmission rights of way | 1,657,530 |
| 1328 | Transmission compressing station structures | 1,466,102 |
| 1329 | Transmission measuring station structures | 133,310 |
| 1330 | Transmission other structures | 113,341 |
| 1331 | Transmission compressing station equipment | 8,048,910 |
| 1332 | Transmission measuring station equipment | 759,625 |
| 1333 | Transmission line equipment | 39,432,331 |
| 1334 | Transmission other equipment | 5,633 |
| [fol. 401] | | |
| 1376 | General other land | 3,655 |
| 1379 | General other structures | 94,687 |

| Number and title of account | Reproduction cost less depreciation |
|---|---|
| 1380 General office equipment | 106,035 |
| 1381 General store equipment | 1,805 |
| 1382 General shop equipment | 23,084 |
| 1384 General stable equipment | 568 |
| 1384 General garage equipment | 81,448 |
| 1385 General laboratory equipment | 8,202 |
| 1386 General telephone and telegraph system | 415,070 |
| 1387 General tools and implements | 44,070 |
| 1388 General other equipment | 21,832 |
| | $58,077,111 |
| Preliminary organization expense | $480,008 |
| Engineering and superintendence during construction | 2,881,000 |
| Administration and legal expense during construction | 304,084 |
| Taxes during construction | 875,171 |
| Interest during construction | 3,883,282 |
| Miscellaneous construction expenditures | 608,169 |
| Cost of financing | |
| Working capital | 775,000 |
| Materials and supplies | 628,675 |
| Going-concern value | 2,000,000 |
| Gas in lines | 22,000 |
| Gas leases | 2,874,390 |
| Rate base | $73,409,190 |

The following observations may be made with reference to the above accounts: In accounts number 1307 and 1327 the commission arrived at the price of $1.47 per rod by taking actual acreage cost on 31 per cent of right of way and damage cost shown in the record as being $1.08 plus the agreed 10 cents per rod for expense of abstracting and recording, plus 22 cents per rod for expense of acquisition, plus 7 cents per rod for engineering, which is at the rate of 5 per cent. There is nothing in the record contrary to the above that warrants the setting aside of the findings of the commission.

Regarding account 1312, it seems to me that the sum of $57,235 deducted by the commission on the legal theory then

advanced is not tenable and that said sum should be restored. Likewise the item of $84,318 should be restored since the engineer for the commission for reasons appearing in the evidence omitted certain items in his calculations which properly belonged therein. I therefore have con- [fol. 402] cluded and found that value of account 1312 should be fixed at $1,294,710.

In relation to account 1314, it might appear that engineer Black's figure is an estimate based upon an arbitrary figure of 50 per cent of the depth of main lines for pipe lines and that Eastman, who testified for the company, was giving evidence from actual size, but a close examination discloses that Eastman's unit prices which he was applying to field lines were not in accordance with the actual depth as shown by inspection, but that with the exception of field ditches excavated by trench machines he applied to his calculations of quantities the width and depth of ditches set forth in exhibit 73, as an average of all underground field pipe lines. I find nothing in the record to warrant setting aside the finding of the commission on this account number 1314.

Considering accounts 1325 and 1328 and 1331, which among other properties, dealt with the Hog Shooter property, station and equipment, account 1325, being as to land owned in fee except general land, account 1328 relates to station structures, and account 1331 relates to station equipment. In this connection it may be said that the argument advanced that between February, 1931, when the company for taxing purposes returned the Hog Shooter property as abandoned, and July, 1931, when the commission ordered the hearing, that the discovery of new gas fields made the Hog Shooter station available, although still not in use during the hearing, does not favorably impress me and I therefore conclude that $2,000 should have been deducted for the Hog Shooter property in account 1325, making the account valuation $145,202 and that $49,560 should have been deducted for Hog Shooter station structure in account number 1328, making the account valuation $1,466,102, and that in account 1331, the Hog Shooter equipment in the amount [fol. 403] of $414,925 should have been deducted, making the account valuation $8,048,910.

Considering account 1333, the per cent condition of the property found to be 90.1 per cent by the commission and the cost of rock excavation as found by the commission and

approved by the majority opinion and in that I concur, leaving only the quantities of rock excavated to be considered and at the threshold of that consideration permit me to state that I agree with the majority that the overcuts should be excluded. In connection with quantities of rock excavated, it should be noted that since the hearing by the commission and before the trial by this court certain inspections were made on one line and the result of such inspection was introduced in evidence at the trial herein. But an examination of that evidence so introduced discloses nothing that will warrant this court in disturbing the finding of the commission in account number 1333, to wit, $39,432,331.

Considering other valuations I have discussed fully gas leases valued at $2,874,390 and the going concern value fixed at $2,000,000.

I concur with the majority that cost of financing should not be included in the rate base.

There remains, therefore, only the following items, to wit: preliminary and organization expense, engineering and superintendence during construction, administration and legal expense during construction, miscellaneous construction expenditures, taxes during construction and interest during construction.

Elsewhere in this opinion I have approved the principle of averaging the values as well as the earnings during the test period, but it should be noted that the valuations set out in the opinion are not average values. They are values of September 1, 1931. Using the valuation found as of that date, to wit, $73,409,190, I find that the plaintiff has failed to show that the 30-cent rate fixed by the commission is confiscatory.

[fol. 404] Under the 40-cent rate the Cities Service Gas Company is earning 8.96 per cent a year upon the present value of its properties.

I find that on the valuation of $73,409,190 and at a rate of 30 cents the return would be 6.41 per cent. If averaged over a period for the calendar year 1930 and the year from June 30, 1930, to June 30, 1931, and the year from June 30, 1931, to June 30, 1932, the return at 30 cents would be 6.849 per cent.

The record shows that by far the largest part of the product handled by the plaintiff in this territory is "industrial gas" which is sold to individual consumers at an average of about 15 cents per M. C. F. A little more than one-third of the city gate rate to the distributing companies 40 cents. Part of this product actually sold to "industrial consumers," and part to "domestic consumers." The industrial consumer (ordinarily) is one who uses a continuous supply of the product through the twenty-four hour period, thereby taking the "off peak" load. The domestic consumer is the housewife, office or mercantile establishment which (ordinarily) uses the supply during the day but not at night.

The rule is that the price for gas should never be unnecessarily low to some consumers while high to others. It should always be high enough to avoid loss to the utility. Special rates for a large portion of the company's output can be justified only upon the ground that they contribute to the public advantage. Discrimination in price based solely on amounts consumed by different patrons cannot be justified, and rebates to certain businesses only because they use a large amount of gas is discriminatory.

Unless the lower rate can be justified upon the ground that it contributes to the general public advantage, the company and not the consumer must bear the loss if one occurs through that class of business. Of course, a schedule of rates contrived for the purpose of selling gas in order that [fol. 405] industries using it may operate more economically than can be done with other fuels may, under some conditions, furnish sufficient grounds for a differential rate. It should be clear, however, that the rate named is not a losing one, and that it will increase the company's profits. (The burden of showing this is on the utility). Differentials of this kind afford no justification for a practice which seeks to charge a large consumer a low price and a small consumer a higher price merely because of a difference in size.

All such considerations should be included in the standard schedule in order that all customers, or possible customers having similar conditions, will receive service at similar rates. A company is not justified in transferring any considerable portion of the costs from one class of

patrons to another class. Schedules should be arranged so that as near as possible each patron will pay his fair share of the cost. No rate should be established unless it provides some profit—that is, some return over and above the costs of operation.

There can be no possible justification for the company to depart from its published schedule of prices, or to give any advantage, directly or indirectly, to one customer not offered to others enjoying or seeking the company's service under like conditions.

If the so called industrial business pays a sufficient profit to bear its part of the load, its part of the upkeep of the general investment, a lower rate is allowable, but, as I see it, the burden is upon the utility to show that such service is self sustaining. In case of loss the utility should not expect the domestic consumer to sustain the industrial consumer's part of the investment.

In the instant case, the increased use of industrial gas has not been manifest in any reduction to the domestic consumer. The plaintiff has insisted and still insists on the gate-rate charge of 40 cents—so that increased industrial business has not led to reductions.

[fol. 406] It appears to be a matter of common knowledge that the distributing companies contract, sell and deliver gas also to some domestic consumers at what appear to be discriminatory rates. They do this apparently on the theory that it is justified in meeting competition with other forms of fuel. This practice of furnishing gas to domestic consumers, such as large mercantile stores and hotels, at rates of from 10 to 17 cents per M. C. F., while charging other individual domestic consumers rates ranging from 75 cents to $1.50 per M. C. F., may amount to unlawful discrimination. This question has not been briefed and I express no opinion thereon. It is one which might well warrant the conclusion that the Doherty companies are not in court with clean hands, and for that additional reason their prayer for equitable relief should be denied. A utility procures its charter and operates through sufference of the state. Rates for its product are allowed and approved by the state's regulatory body. In this instance, the Public Service Commission allows and approves local rates to the consumers. The companies involved here having applied for and procured approval of such rates are bound thereby

and for them to follow the practice of disregarding the approved schedule of rates in favoring some consumers above others, is contrary to law. (See R. S. Kan. 66-107, 66-108, 66-109; Empire Natural Gas Co. v. Thorp, 121 Kan. 116; Kansas Electric Power Co. v. Thomas, 123 Kan. 321.) It should not be tolerated, much less have the approval of this court.

If it be argued that so-called industrial sales are not made at a loss, that there is an actual profit on sales to individual consumers at rates as low as from 10 to 15 cents per M. C. F., it certainly is unreasonable to hold that a rate of 30 cents at the city gates to the distributing companies is confiscatory. The distributing company represents all of the consumers collectively, and the argument that it can dispense gas to one of its patrons at from 10 to 15 cents [fol. 407] per M. C. F. at a profit and that a rate of 30 cents to it at the city gates for all its patrons collectively is confiscatory, does not appeal to my reason. The burden rests upon the utility to show clearly that the rate (30¢) is confiscatory. This it has failed to do.

Knoxville v. Water Co. (212 U. S. 1, at page 16), Mr. Justice Moody, speaking for the court, said:

"If a company of this kind chooses to decline to observe an ordinance of this nature and prefers rather to go into court with the claim that the ordinance is unconstitutional, it must be prepared to show to the satisfaction of the court that the ordinance would necessarily be so confiscatory in its effect as to violate the constitution of the United States. In Ex parte Young, 209 U. S. 123, the last word of caution by this court was said (p. 166): Finally it is objected that the necessary result of upholding this suit in the circuit court will be to draw to the lower federal courts a great flood of litigation of this character, where one federal judge would have it in his power to enjoin proceedings by state officials to enforce the legislative acts of the state, either by criminal or civil actions. To this it may be answered, in the first place, that no injunction ought to be granted unless in a case reasonably free from doubt. We think such rule is, and will be, followed by all the judges of the federal courts. The same thought, in effect, was expressed in San Diego Land & Town Company v. National City, 174 U. S. 739, 754; judicial interference should never occur unless the case presents, clearly and beyond all doubt, such a

flagrant attack upon the rights of property under the guise of regulations as to compel the court to say that the rates prescribed will necessarily have the effect to deny just compensation for private property taken for the public use?"

The parties to this litigation have asked that the case be considered on its merits and a final determination reached. On page 147 of its brief the plaintiff says "We believe it to be most desirable that this court should examine the facts, as well as the law and give to the people the benefit of its authoritative decision upon the real question at issue."

In accordance with this expressed desire, the writer of this opinion has made an investigation of the facts and the [fol. 408] law and is of the opinion that the plaintiff has failed to show that the orders in question, made by the Public Service Commission of Kansas, are unlawful or confiscatory. In accordance with the desire of the parties, I have prepared and filed full findings of fact and conclusions of law in accordance with the views herein expressed. The bills should be dismissed.

[File endorsement omitted.]

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[fol. 409] IN UNITED STATES DISTRICT COURT

SEPARATE FINDINGS OF HOPKINS, DISTRICT JUDGE—Filed Jan. 14, 1933

## Findings of Fact

For a long period of years, more than twenty, Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has maintained a complete organization for the design, construction, operation and development of public utilities, and oil and natural gas properties. This organization is composed of experienced executives, financial advisors, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technicians, experts, accountants, operators and lawyers. There are approximately 1,667 employees. In this organization Mr. Doherty maintains departments for the purchase, sale, promotion and transfer of

stocks of his various corporations, a foreign oil department; marine and tank car department; and oil production and refining department; a real estate division chiefly concerned with New York real estate, and maintains a London office.

II

The parties to this litigation are all units or corporations of the Doherty organization, and all have to do in some degree with the production, transportation and sale of natural gas to consumers of Kansas.

III

On July 2, 1931, an order was entered by the Public Service Commission of Kansas, on its own initiative, directed to the plaintiffs herein, except the Cities Service Gas Company, finding that the reasonableness of all contracts with, and charges made to, the respondents by corporations owning the stock of the plaintiffs, and of the contracts between Henry L. Doherty & Co. and respondents should be inquired into; the respondent distributing companies were ordered to show cause why payments made under such contracts, [fol. 410] if found to be unreasonable, should not be disallowed as operating expenses. A copy of said order is Exhibit A attached to the bills of complaint of the distributing companies.

IV

Pursuant to such order, extensive hearings were held. The properties of the Cities Service Gas Company, situated in five states were appraised by engineers for both parties and valued by the Commission. Findings and conclusions were filed by the Commission.

A petition for rehearing was filed, allowed, rehearing had, and the orders entered which are now submitted for review to this court.

V

The citizenship and official position of the parties are as stated in the bills of complaint. There is diversity of citizenship, a substantial federal question in each of the cases and more than $3,000 in controversy.

VI

The plaintiff distributing companies were engaged in the sale and distribution of natural gas to domestic and industrial consumers of 128 cities and towns in Kansas, procuring their gas from another of the Doherty units the Cities Service Gas Company. The Cities Service Gas Company, through Henry L. Doherty, has a practical monopoly on the sale of gas to the distributing companies. The arrangement being that the pipe line company will supply the present needs of the distributing companies at 40 cents per thousand cubic feet, delivered to their mains. This 40 cent rate is a private contract between the affiliated Doherty corporations.

VII

Except for qualifying shares, the common stock of the distributing companies is owned by the Gas Service Company, the stock of which in turn is owned by the Cities Service Company. The common stock of the Cities Service Gas Company [fol. 411] is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. The Empire Gas & Fuel Company has a preferred stock issue outstanding in the hands of the public. Henry L. Doherty owns 35 per cent of the voting stock of the Cities Service Company. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of all the corporations, including the Cities Service Gas Company. The distributing companies do not deal at arm's length with either the Cities Service Gas Company or Henry L. Doherty.

VIII

The Cities Service Gas Company was organized in 1926. It took over the physical properties of five pipe-line companies, having a plant investment account at that time of $52,182,525.98. These pipe-line companies served many communities in Oklahoma, Kansas and Missouri. The companies taken over were integrated, so that the gas could be run from the mains of one system into that of another, and the supply thereby made more dependable and economical. Natural gas had long been used for lighting and cooking in most of these cities and towns.

There are extensive and prolific gas fields at Amarillo, Texas, and Hugoton, Kansas. It is a matter of common knowledge these fields are being enlarged and extended so that the supply is dependable for all uses, for a long period of time. The Cities Service Gas Company now has an adequate and dependable supply of gas, available at all times at the city gates. Mr. Doherty, through the Cities Service Company, acquired the distributing companies in order to meet keen competition.

IX

[fol. 412] The distributing companies, as units of the Doherty organization, have each entered into a contract with the Henry L. Doherty Company which provides for services as follows:

1. Personnel (i. e., experienced executives and operators).
2. Executive service.
3. General accounting service.
4. Statistical service.
5. Purchasing service.
6. Designing and construction engineering.
7. Financial service.
8. Securities department.
9. Valuation.
10. Tax departments.
11. New business department.
12. Technical and research department.

X

The Gas Service Co., another Doherty unit, with offices in Kansas City, Mo., has a contract with the distributing companies similar in many respects to the one above set out in finding number nine. It provides that it furnish services as follows:

1. Furnish all administrative and executive service.
2. Financial aid and advice.
3. Purchasing and warehousing.
4. Engineering and operating supervision.
5. All legal services.
6. All insurance purchasing.
7. All general accounting and reports.

8. Supervision and handling of all tax matters.
9. Handling of all pay rolls.
[fol. 413] 10. Making of all audits and auditing reports.
11. Make all governmental and regulatory commission reports.
12. Supervision of all new business operations.
13. Make all vouchers and disburse funds.
14. Supervise and direct all public relations work.
15. Do all general and policy advertising.
16. Make all valuations and rates and handle all matters pertaining to rate litigation, and routine matters with regulatory bodies.
17. Make and follow up all construction and financial budget.

The Commission found that the amounts paid by the distributing companies under this contract with the Gas Service Company were not unreasonable, but refused to approve payments on the contracts set out in finding nine, because of duplication.

## XI

The activities of Henry L. Doherty & Company embrace many matters not covered by the 1¾ per cent contract, the expense of which is not a proper operating charge of the distributing companies. These activities are: The promotion, sale and transfer of securities of the Cities Service Company and its affiliates. No securities of the distributing companies have been marketed by Henry L. Doherty & Company, and if they are, the contract provides for a separate fee for such services. The production, sale and transportation of oil and the handling of New York real estate are unrelated activities. The record discloses no reason for these distributing companies maintaining a London office. The consumers of natural gas have no interest in Mr. Doherty's oil or stock business, and his private businesses ought not to be thrown together with the business of serving the public, the expenses of all hopelessly intermingled.

On September 1, 1931, there were properties of the City Service Gas Company used and useful in the public service, as follows:

[fol. 414]

| Number and title of account | Reproduction cost less depreciation |
|---|---|
| 1307 Production—rights of way | $55,982 |
| 1310 Production—field measuring station structures | 35,909 |
| 1311 Production—other structures | 47,876 |
| 1312 Production—gas-well construction | 1,294,710 |
| 1313 Production—gas-well equipment | 658,439 |
| 1314 Production—field-line equipment | 3,126,159 |
| 1315 Production—field measuring station equipment | 265,746 |
| 1316 Production—drilling and cleaning equipment | 27,908 |
| 1317 Production—other equipment | 1,333 |
| 1325 Transmission—land | 145,202 |
| 1327 Transmission—rights of way | 1,657,530 |
| 1328 Transmission—compressing station structures | 1,466,102 |
| 1329 Transmission—measuring station structures | 133,310 |
| 1330 Transmission—other structures | 113,341 |
| 1331 Transmission—compressing station equipment | 8,048,910 |
| 1332 Transmission—measuring station equipment | 759,625 |
| 1333 Transmission—line equipment | 39,432,331 |
| 1334 Transmission—other equipment | 5,633 |
| 1376 General—other land | 3,655 |
| 1379 General—other structures | 94,687 |
| 1380 General—office equipment | 106,035 |
| 1381 General—store equipment | 1,805 |
| 1382 General—shop equipment | 23,084 |
| 1383 General—stable equipment | 568 |
| 1384 General—garage equipment | 81,448 |
| 1385 General—laboratory equipment | 8,202 |
| 1386 General—telephone and telegraph system | 415,070 |
| 1387 General—tools and implements | 44,979 |
| 1388 General—other equipment | 21,832 |
| | $58,077,111 |

| Number and title of account | Reproduction cost less depreciation |
|---|---|
| Preliminary organization expense | 480,008 |
| Engineering and superintendence during construction | 2,881,000 |
| Administration and legal expense during construction | 304,084 |
| Taxes during construction | 875,171 |
| Interest during construction | 3,883,282 |
| Miscellaneous construction expenditures | 608,169 |
| Cost of financing | |
| Working capital | 775,000 |
| Materials and supplies | 628,675 |
| Going-concern value | 2,000,000 |
| Gas leases | 2,874,390 |
| Rate Base | $73,409,100 |

The following observations may be made with reference to the above accounts. In accounts number 1307 and 1327, the commission arrived at the price of $1.47 per rod by taking actual acreage cost on 31 per cent of right of way and damage cost shown in the record as being $1.08 plus agreed 10 cents per rod for expense of abstracting and recording, plus 22 cents per rod for expense of acquisition, plus 7 cents per rod for engineering, which is at the rate [fol. 415] of 5 per cent. There is nothing in the record contrary to the above that warrants the setting aside of the findings of the commission.

Regarding account 1312, it seems to me that the sum of $57,235, deducted by the commission on the legal theory there advanced is not tenable and that said sum should be restored. Likewise the item of $84,318 should be restored, since the engineer for the commission, for reasons appearing in the evidence, omitted certain items in his calculations which properly belonged therein. I therefore have concluded and found that value of account 1312 should be fixed at $1,294,710.

In relation to account 1314, it might appear that engineer Black's figure is an estimate based upon an arbitrary figure of 50 per cent of the depth of main lines for pipe lines and that Eastman, who testified for the company, was giving evidence from actual size, but a close examination discloses

that Eastman's unit prices which he was applying to field lines were not in accordance with the actual depth as shown by inspection, but that with the exception of field line ditches excavated by trench machines, he applied to his calculations of quantities the width and depth of ditches set forth in exhibit 73, as an average of all underground field pipe lines. I find nothing in the record to warrant setting aside the finding of the commission on this account number 1314.

Considering accounts 1325 and 1328 and 1331, which, among other properties, dealt with the Hog Shooter property, station and equipment account 1325, being as to land owned in fee except general land, account number 1376, account 1328 relates to station structures, and account 1331 relates to station equipment. In this connection it may be said that the argument advanced that between February, 1931, when the company for taxing purposes returned the Hog Shooter property as abandoned, and July, 1931, when the commission ordered the hearing, that the discovery of [fol. 416] new gas fields made the Hog Shooter station available, although still not in use during the hearing, does not favorably impress me, and I therefore conclude that $2,000 should have been deducted for the Hog Shooter property in account 1325, making the account valuation $145,202, and that $49,560 should have been deducted for Hog Shooter station structure in account number 1328, making the account valuation $1,466,102, and that in account 1331 the Hog Shooter equipment in the amount of $414,325 should have been deducted, making the account valuation $8,048,810.

Considering account 1333, the per cent condition of the property found to be 90.1 per cent by the commission, and the cost of rock excavation as found by the commission and approved by the majority opinion, and in that I concur, leaving only the quantities of rock excavated to be considered, and at the threshold of that consideration permit me to state that I agree with the majoriy that the overcuts should be excluded in connection with quantities of rock exeavated. It should be noted that since the hearing by the commission and before the trial by this court certain inspections were made on one line and the result of such inspection was introduced in evidence at the trial herein. But an examiation of that evidence so introduced discloses

nothing that will warrant this court in disturbing the finding of the commission in account number 1333, to wit $39,432,331.

Considering other valuations, I have discussed fully gas leases valued at $2,874,390 and the going-concern value fixed at $2,000,000.

I concur with the majority that cost of financing should not be included in the rate base.

There remains, therefore, only the following items, to wit: preliminary and organization expense, engineering and superintendence during construction, administration and [fol. 417] legal expense during construction, miscellaneous construction expenditures, taxes during construction and interest during construction.

Elsewhere in this opinion I have approved the principle of averaging the values as well as the earnings during the test period, but it should be noted that the valuations set out in the opinion are not average values. They are values of September 1, 1931. Using the valuation found as of that date, to wit, $73,409,190, I find that the plaintiff has failed to show that the 30 cent rate fixed by the commission is confiscatory.

Under the 40 cent rate the Cities Service Gas Company is earning 8.96 per cent a year upon the present value of its properties.

I find that on the valuation of $73,409,190 and at a rate of 30 cents the return would be 6.41 per cent. If averaged over a period for the calendar year 1930 and the year from June 30, 1930, to June 30, 1931, and the year from June 30, 1931, to June 30, 1932, the return of 30 cents would be 6.849 per cent.

Richard J. Hopkins, District Judge.

## Conclusion

I conclude that the Plaintiff has not shown that the order of the Public Service Commission should be set aside and that the Bills should be dismissed.

[File endorsement omitted.]

[fol. 418] IN UNITED STATES DISTRICT COURT

DECREE—Filed Jan. 28, 1933

Now, on this 28th day of January, 1933, this case came on for decision pursuant to its previous submission to the court, the plaintiffs appearing by: James W. Finley, R. E. Cullison, Chas. Frueauff, Robt. S. Sloan, Fred Robertson, J. O. Emerson, Robt. Garver, Robt. Stone, and the defendants appearing by Walter T. Griffin, Chas. D. Welch, Harry Castor, Chas. W. Steiger and E. H. Hatcher, and thereupon, upon consideration thereof, it was ordered, adjudged, and decreed as follows:

(1) That the temporary injunction heretofore issued against the Attorney General of the State of Kansas be dissolved.

(2) That the temporary injunction restraining the defendant, The Public Service Commission of the State of Kansas, from enforcing its order of August 31, 1932, in so far as it pertains to the 1¾ per cent payment to Henry L. Doherty & Company, of the gross revenues of the distributing companies, be dissolved and that the application of plaintiffs for an injunction as to that part of said orders be denied and dismissed.

(3) That the defendants, the Public Service Commission of the State of Kansas, and the members thereof, and Roland Boynton, Attorney General of the State of Kansas, and each of them, their agents, servants, and employees, and all other persons acting under or through their authority, be and they are hereby permanently enjoined and restrained in the enforcement and execution of the provisions of two certain orders of said Public Service Commission dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above named cases, should cease to set up on their books any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer, and, insofar as they and/or either of them require that effective September 1, 1932, and until a hearing is held and an order

[fol. 419] issued, the said distributing companies should charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. should deduct the difference between what the distributing companies were then paying at the city gate and 30 cents per M. C. F., and should pass this difference on to the consumer.

(4) That the costs in this court in these cases consolidate, be taxed one-half to the defendant, The Public Service Commission of the State of Kansas, and one-half to the plaintiffs.

The Public Service Commission of the State of Kansas and Roland Boynton, as Attorney General, defendants herein, hereby object and except to that part of finding number 13 which states:

"The present values are, on the extensive constructions of the last few years, less than the prudent investment therein. * * *"

and to each of findings Nos. 14, 16, 17, 18, 19, 20, 21 and to the conclusion of law No. 1 and to that part of this decree which enjoins the Public Service Commission of the State of Kansas in reference to its said orders, and exceptions thereto, are hereby allowed.

Plaintiffs and each of them object and except to findings Nos. 14 and 16 and exceptions thereto are hereby allowed.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge.

Approved.

Jas. W. Finley, R. E. Cullison, Fred Robertson, R. D. Garver, Robert Stone, Attorneys for Plaintiffs. Chas. D. Welch, Chas. W. Steiger, E. H. Hatcher, Roland Boynton, Walter T. Griffin, Attorneys for Defendants.

[File endorsement omitted.]

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[fol. 420] IN UNITED STATES DISTRICT COURT

ORDER SUBSTITUTING PARTIES DEFENDANT—Filed April 19, 1933

This matter coming on for hearing on the Motion of the State Corporation Commission and Homer Hoch, Jesse W.

Greenleaf and Ernest E. Blincoe, as members, that they be [fol. 421] substituted as parties defendant in the above entitled case, and the court being duly advised, finds that said motion should be sustained.

It is, therefore, by the Court ordered that the State Corporation Commission for the State of Kansas, and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe, as members of said Commission, be and they hereby are substituted as parties defendant in the above entitled action in the place of the Public Service Commission for the State of Kansas, and Jesse W. Greenleaf, Thurman Hill and Chas. W. Campbell, Commissioners.

Orie L. Phillips, Geo. T. McDermott, Richard J. Hopkins, Judge.

[File endorsement omitted.]

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[fols. 422 & 423] In United States District Court

In Equity. No. 1637-N

[Titles omitted]

And the following cases consolidated therewith:

In Equity. No. 1638-N. In Equity. No. 1639-N. In Equity. No. 1640-N. In Equity. No. 1641-N. In Equity. No. 1642-N. In Equity. No. 1643-N. In Equity. No. 1644-N. In Equity. No. 1645-N. In Equity. No. 1646-N.

[fol. 424] Petition for Appeal, Assignment of Errors, and Prayer for Reversal.—Filed April 18, 1933

Petition for Appeal

To the Honorable District Court of the United States for the District of Kansas, First Division:

Your petitioners, The State Corporation Commission of Kansas, and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe, as members, successors to and substituted for The Public Service Commission of the State of Kansas, and

Jesse W. Greenleaf, Thurman Hill and Chas. W. Campbell, as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, the defendants in the above consolidated cases, considering themselves aggrieved by the decree entered in the above entitled cause on the 28th day of January, 1933, for the reason specified in the assignment of errors which is filed herewith, pray that they may be permitted to take an appeal therefrom to the Supreme Court of the United States at Washington.

Your petitioners further desire that an order be made fixing the amount of appeal bond herein for costs.

[fol. 425] ASSIGNMENT OF ERRORS

And your petitioners, The State Corporation Commission of Kansas, and Homer Hoch, Jesse W. Greenleaf, and Ernest E. Blincoe, successors to and substituted for The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and Chas. W. Compbell, as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, defendants, assign the following errors in the record and proceedings in the said case:

1. The District Court of the United States for the District of Kansas, First Division, erred in permanently enjoining and restraining the enforcement and execution of the provisions of the two certain orders of The Public Service Commission as dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above cases, should cease to set up on their books any payments made to the Cities Service Gas Company for mainline town border gas in excess of 30¢ per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2. The Court erred in refusing to dismiss the plaintiff's bills of complaint and in granting the petitioners any relief.

3. The Court erred in their opinion and findings declaring the order of The Commission was, as to any part, unreasonable and would, if not enjoined, confiscate the property of these plaintiffs.

[fol. 426] 4. The Court erred in not accepting the finding of facts, declarations of law and dissenting opinion of Hon-

orable Richard J. Hopkins, as declaratory of the law and facts controlling in this case.

5. The Court erred in finding:

"The present values are on the extensive constructions of the last few years, less than the prudent investment therein * * *" (Finding 13).

6. The Court erred in finding the rate base to be $82,380,583. (Finding 14).

7. The Court erred in finding the present value of the Cities Service Gas Company's rights of way to be $1.62 per rod and erroneously increased the valuation in the amount of 22¢ per rod on rights of way, a total increase of $266,693.00. (Finding 14, Account 1307, 1327).

8. The Court erred in adding $84,318 to the cost of gas well construction as found by the Commission. (Finding 14, Account 1312), and thereby erroneously increased the rate base in said amount.

9. The Court erred in adding $397,017 to the value found by the Commission for production field line equipment, (Finding 14, Account 1314), and thereby erroneously increased the rate base in said amount.

10. The Court erred in finding that the Hogshooter compressor station was used and useful, and in adding to the value found by the Commission, $2,000 for land at the Hogshooter station, $49,560 for compressor station, and in adding the value of the equipment at the Hogshooter station in the amount of $414,925.00. (Finding 14, Accounts 1325, 1328, 1331.)

[fol. 427] 11. The Court erred in finding that the value found for Account 1333 by the Commission should be increased from $39,432,331 to $40,232,331, because the amount of rock excavation in the pipe-line construction allowed by the Commission was too law. (Finding 14).

12. The Court erred in finding that going concern value should be placed in the rate base at $5,000,000 and the value found by the Commission increased $3,000,000; (Finding 14).

13. The Court erred in finding that 1,261,000 acres of gas leases owned by The Cities Service Gas Company were used

and useful, and should be included in the rate base including developed, proven, probable and prospective acreage, and erred in increasing the acreage allowed as used and useful and in valuing the same at $5,727,272. (Finding 14.)

14. The Court erred in finding that the net income available for return amounted to only $5,800,327, and in including a portion of the rate expense of the present investigation as a proper item of expense in arriving at the net earnings available for return. (Finding 16.)

15. The Court erred in allowing $329,917 as annual replacement requirements on account of rentals on unproducing leases. (Finding 16.)

16. The Court erred in finding that $174,747.74 was necessary as an annual allowance for dry hole expense. (Finding 16.)

[fol. 428] 17. The Court erred in its finding and conclusion that The Cities Service Gas Company is earning an annual return of only 7.11 per cent on the present valuation of its property. (Finding 17.)

18. The Court erred in its finding and conclusion that approximately 8 per cent return upon present valuation is necessary for the Cities Service Gas Company at the present time, and that a return substantially lower than that would be confiscatory; and erred in its finding that if abnormality is considered the return must be increased and not decreased. (Finding 18.)

19. The Court erred in its finding that under the orders of the Commission, the return upon the properties of The Cities Service Gas Company dedicated to the public use would be 4.8 per cent; and erred in its finding that such rate under present conditions is confiscatory. (Finding 19.)

20. The Court erred in its finding that if the distributing companies are compelled to pay 40c per thousand cubic feet for gas at the city gates and to base their rates to consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses applicable to depreciation and return. (Finding 20.)

21. The Court erred in its conclusion of law that that portion of the first order of the Commission, made August [fol. 429] 31, 1932, providing that the distributing companies should give no consideration to the payments for gas at the city gates in excess of 30c per thousand cubic feet in fixing the rate for domestic consumers, should be permanently enjoined. (Conclusion of law, 1).

22. The court erred in its conclusion that forty cents per thousand cubic feet for gas at the city gates is a reasonable charge. (Opinion.)

[fol. 430] Prayer and Reversal

For which errors the petitioners, The State Corporation Commission of the State of Kansas, and Homer Hoch, Jazza W. Greenlief and Ernest E. Blincoe, as member of said Commission, and Roland Boynton, as Attorney General of the State of Kansas, pray that said judgment and decree of the District Court of the United States for the District of Kansas, First Division, dated January 28, 1933, in the above entitled cause, be reversed in so far as it enjoins the enforcement of any part of the Commission's said orders, and a judgment rendered in favor of said petitioners, and for costs.

Chas. D. Welch, Louis R. Oates, Chas. W. Steiger,
E. H. Hatcher, Roland Boynton, Atty General,
Counsel for Appellants.

Received copy of the foregoing petition for appeal, assignment of errors and prayer for reversal, this 12th day of April, 1933.

Robt. D. Garver, Robt. Stone, Counsel for Appellees.

[fol. 431] In United States District Court

Order Allowing Appeal. Filed April 19, 1933

The Appellants in the above entitled suit and each of them, having prayed for the allowance of an appeal in this cause to the Supreme Court of the United States from the judgment and decree made and entered in the above en-

titled suit by the District Court of the United States for the District of Kansas, First Division, on the 28th day of January, 1933, and having presented and filed their petition for appeal, assignment of error, and prayer for reversal pursuant to the statutes and the rules of the Supreme Court of the United States in such case made and provided;

It is now here ordered that an appeal be, and the same is hereby allowed to the Supreme Court of the United States from the District Court of the United States for the District of Kansas, First Division, in this cause as provided by law; and it is further ordered that the Clerk of the court appealed from shall prepare and certify a transcript of the record, proceedings, judgment and decree in this cause and transmit the same to the Supreme Court of the United States.

And it is further ordered that security for costs on appeal be fixed in the sum of $5,000.00, and that bond be given therefor.

Dated this 19th day of April, 1933.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, U. S. District Judge.

[File endorsement omitted.]

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[fols. 432-434] Bond on appeal for $5,000, approved and filed April 18, 1933, omitted in printing.

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[fol. 435] IN UNITED STATES DISTRICT COURT

Condensed Statement of Evidence Essential to Decision on Question Presented on Appeal—Filed May 15, 1933

The case was tried below to a statutory three-judge court, the evidence introduced consisting of the entire record of evidence introduced by all parties before the Public Service Commission of Kansas, such record consisting of approximately 3000 pages of testimony and 103 exhibits, and certain additional stipulations and affidavits considered as evidence by the parties.

Issues

The issues for determination before the Commission and the Court below were as follows:

1. The reasonableness of the price charged by the Cities Service Gas Company to the several distributing companies, respondents before the Commission and plaintiffs below.

2. The reasonableness of the contract between Henry L. Doherty & Company and said several distributing companies under which they paid for certain services, 1¾ per cent of their gross revenue.

3. The reasonableness of the contract between said several distributing companies and The Gas Service Company.

[fol. 436] This appeal concerns only issue No. 1, above, as to the reasonableness of the price charged for gas at the city gates of the respective cities served by the appellees, neither party having appealed from the decision of the court below as to other issues.

The Court below in its findings of fact considered the several elements entering into the rate base of the Cities Service Gas Company under certain account numbers and headings and this condensed statement of the evidence will follow such divisions of the subject, so far as possible.

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Stipulation as to Certain Facts, Testimony, etc.

The parties stipulated before the District Court as follows:

"It is hereby stipulated by the parties that the three instruments marked respectively, A. B. and C. by the reporter are the three orders made by the Texas Railroad Commission with regard to permissible takes from wells in the Amarillo field of Texas.

"It is further stipulated that a suit has been brought in the Federal Court in Texas, contesting the validity of this order and that the same was restrained by the Court, set for hearing in the matter on application for temporary injunction, that subsequent to the issuance of said restrain-

ing order the Texas Commission set aside the order of September 15th, for the reasons set out in Exhibit 3.

"It is agreed by the parties that the witness, H. O. Caster, a member of the Executive Committee of Henry L. [fol. 437] Doherty & Company and the head of the Natural Gas Division of that organization will testify that all leases in present gas reserves of the Cities Service Gas Company were purchased in the exercise of the bona fide business judgment of himself and other members of said Executive Committee, and the managing officers of the Cities Service Gas Company as necessary to secure an adequate supply of gas for the Cities Service Gas Company and were not purchased for speculation.

"It is further agreed by the parties that the witness, Ross M. Stuntz, Superintendent of Gas Production of the Cities Service Gas Company, will testify that all of the present reserves of the Cities Service Gas Company are, in his opinion, presently necessary to the Cities Service Gas Company; that at the present time the Cities Service Gas Company owns 111,574 acres of producing leases, that 5 percent of all gas transported through the Cities Service Gas Pipe Line System is necessary for leakage and the operation of compressor stations and cannot be figured in deliveries to consumers; that in computing the number of acres comprising the above figure of 111,574 as representing producing leases, the computation was made on the basis of one well rendering a lease developed, without regard to the size of the lease, and that if a well is located on an eighty acre lease, eighty acres are included as productive and if the well is located on a thousand acre lease the same is true, except in the Osage Nation of Oklahoma where the company owns one lease of 181,120 acres, of which 2,480 acres are classed as producing, although there are 14 wells on the 181,000 acres block as a whole. That the above developed acreage is divided between the states as follows: Texas, 97,700 with 60 wells as of September 1, 1931, and 2 additional wells since that time, making a total of 62 wells; Kansas 10,071 acres with 189 wells as of September 1, 1931; Oklahoma 3,613 acres developed with 40 wells as of September 1, 1931.

[fol. 438] "It is further stipulated that the witness, H. O. Caster, will testify that in his bona fide business judgment the contract under which the distributing companies, com-

plainants herein, pay to Henry L. Doherty & Company one and three-fourths percent of their gross revenues is to the best interest of said distributing companies and that services are rendered to said companies which are necessary or advisable to their operations and that such services cannot be procured elsewhere at a less cost to said company, and that the same is true with respect to a like contract between Henry L. Doherty & Company and the Cities Service Gas Company.

"It is further stipulated that the witness F. C. Hamilton will testify that he is familiar with the value and financial experience of the distributing companies, plaintiffs herein, and that the value of their respective properties and their operating experience is as set out in the several bills of complaint of the complainants herein other than the Cities Service Gas Company, to which the Public Service Commission objects on the ground that the testimony is irrelevant, incompetent and immaterial, and further states that it has had no opportunity to investigate this matter or value the property and that it was the intention of the Commission to do so in pursuance of its order set out in plaintiff's bill of complaint at Exhibit 1.

"It is further stipulated that the witness F. C. Hamilton will testify that if the several distributing companies complainants herein are compelled to pay the price they are now paying the Cities Service Gas Company for gas at their respective city gates and are compelled to base their rates to consumers upon the price fixed by order, Exhibit M, they will not be able to make operating expenses, with nothing for return and depreciation on the value of their property, to which testimony the Commission objects [161, 439] on the ground of incompetency, the subject matter not coming in issue until the Commission has made an investigation for the purpose of determining the fair value of the properties owned by the distributing companies and their rate of return.

"It is further stipulated that the witness James A. Emery will testify that he is Vice President and Director of Ford, Bacon & Davis, Inc., engineers; that he was employed by the complainants herein to make a study of the property of the Cities Service Gas Company for the purpose of determining the proper allowance for going value and that in the opinion of said witness going value should

be allowed in a sum between eight and a half and nine million dollars.

"It is further stipulated by the parties that the Exhibit marked 4, which is an abstract of the testimony before the Commission in regard to the contract of Henry L. Doherty & Company *in regard to the contract of Henry L. Doherty & Company* prepared by the parties may be considered by the Court with the eliminations of any statements which appear therein which may not properly be considered as an abstract of the testimony.

"It is further stipulated by the parties that the entire record and all exhibits before the Commission may be considered by the Court herein without regard to whether or not the evidence is abstracted.

"If is further stipulated that the contract between the Cities Service Gas Company and Henry L. Doherty & Company under which it pays one and three-fourths percent of its gross revenue on sales to unaffilliated companies and pipe line customers not served through distributing companies and was entered into in like manner and that H. O. Caster and H. R. Straight, General Manager of Cities Service Gas Company would testify that there is no species of domination or control over Cities Service Gas Company by any person, company or corporation other than [fol. 440] such as necessarily arises by ownership of all voting stock except qualifying shares and by Empire Gas & Fuel Company, and as may be implied, if any, by the management contract above mentioned.

"It is further stipulated that there is no contract between Gas Service Company and Henry L. Doherty & Company, under which it pays them one and three-fourths percent of its gross earnings or any other compensation whatever.

"It is further stipulated that the cost of the leases, sold to the Texhoma and transferred in August, 1931, as shown by the books of the company, is $846,217.72.

"It is further stipulated that all affidavits introduced by any of the parties are subject to objection for relevancy and materiality.

"It is stipulated in connection with the affidavit of H. L. Montgomery that the city gate rate of the Cities Service Gas Company in Oklahoma is 35 cents.

"It is agreed that if the rate established by the Commission in its order Exhibits L. — H., if applied to the

business of the Cities Service Gas Company for the year ending June 30, 1932, would result in a reduction of earnings of $1,926,145.07, leaving net earnings above replacement reserves of $5,935,377.78.

"It is stipulated that exhibit 5 is a photostatic copy of one of the storage leases in effect in the Craig field and that the photostatic copies of checks attached thereto are checks that were paid in connection with said contract.

"It is further stipulated that the same form of contract was executed by all land owners in this field. As to the Eldorado field referred to in the record as the Augusta field the Cities Service Gas Company was the owner of production leases covering all land now used for storage, which leases provided for annual payment per well during such time as gas was used off the premises and that the com- [fol. 441] pany is continuing to pay the land owners the stipulated rental per well the same as if gas were being produced from the sand instead of from storage. There is no additional contract with the land owners who are receiving and accepting their annual rentals the same as if gas was actually being produced. The leases under which the storage field is now held are the ordinary form of oil and gas leases providing for annual rental per well for gas used off the premises.

"It is further stipulated between Cities Service Gas Company and defendants in its case that said company could not continue its business without the patronage of the defendant distributing companies."

It was stipulated between the parties that an agreed statement of facts and agreed abstract of the evidence should be presented to the lower court with the evidence pertaining to each account brought forth and abstracted under each particular account of the valuation to which it pertains. The valuation for a large number of the accounts is not in controversy before the district court and is not in controversy in this appeal.

The parties stipulated as follows:

"The foregoing is agreed to be a correct abstract of the evidence introduced before the Commission in the proceedings in question and all facts herein stated may be considered as shown by the evidence without prejudice to the introduction of additional evidence by any party."

## Agreed Statement of Facts and Evidence

The agreed statement of facts and the agreed abstract of the evidence setting forth the undisputed accounts is as follows:

"In its order of July 20, 1932, the Public Service Commission found the value of the property of the Cities Service Gas Company and associated companies to be $73,051,-[fol. 442] 235.00 as of September 1, 1931.

"In its order of August 3, 1932, the Commission made additions to its previous finding and found the value of this property as of September 1, 1931 to be $73,148,510.00. In making this finding of value, the Commission intended to add $119,275.00 to the value previously found, but by mistake added the sum of $119,275.00 to the figure of $73,029,-235.00 instead of adding it to the figure of $73,051,235.00 as previously found. The correction of this error makes the value of the property of the Cities Service Gas Company, as of September 1, 1931, as found by the Commission, $73,170,510.00.

"On pages 28 and 29 of the opinion, the Commission tabulates by account numbers the several items entering into its valuation as found, and the evidence as hereinafter abstracted will follow the account numbers as tabulated by the Commission and followed in its opinion.

"The witnesses who testified in regard to valuation were F. C. Hamilton, consulting engineer for Henry L. Doherty & Company, and H. L. Eastman, associated with Mr. Hamilton, for the respondents, and E. B. Black, of the firm of Black and Veatch of Kansas City, Missouri, for the Public Service Commission. In the following abstracts these witnesses will be referred to as Hamilton, Eastman and Black. All based their present value on reproduction cost, new, less depreciation.

"Mr. Black testified: 'It was not my idea in making this appraisal or fixing these prices to use the rock bottom price of labor or materials.'

"C. H. Montgomery, the Certified Public Accountant employed by the Commission, testified as to exhibits prepared by him, included in which is the value of the property of the Cities Service Gas Company as shown by its books.

"The correctness of Montgomery's audit is not questioned. As shown in the exhibit offered by him the cost of

the gas leases, owned by Cities Service Gas Company, is $6,573,489.70. This figure is also recited by the Commission in its opinion at page 118. The plant investment and [fol. 443] other assets including leases of Cities Service Gas Company is shown in the same exhibit to be $96,795,538.93 and at page 1970 of the record at $96,795,000.00. This figure includes some leases later sold to the Texhoma Company.

UNDISPUTED ACCOUNTS

"Account No. 1307. Production—Rights of way. In his valuation, Black separated production right of way and transmission right of way, whereas Hamilton included both under Account No. 1327. The testimony of both Black and Hamilton will be abstracted under Account No. 1327.

"Account No. 1310. Production—Field measuring station structures—$35,909.00.

"Account No. 1311. Production—Other structures—$47,876.00.

"Accounts Nos. 1315. Production—Field measuring station equipment—$265,746.00.

"Account No. 1317. Production—Other Equipment—$1,333.00.

"Account No. 1329. Transmission—Measuring Station structures—$133,310.00.

"Account No. 1330. Transmission—Other structures—$113,341.00.

"Account No. 1332. Transmission measuring station equipment—$759,625.00.

"Account No. 1334. Transmission—Other equipment—$5,633.

"Account No. 1379. General—Other structures—$94,687.00.

[fol. 444] "Account No. 1384. General—Garage equipment—$81,448.00.

"Account No. 1386. General—Telephone and Telegraph system—$415.070.00.

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[fol. 445] "ENGINEERING AND SUPERINTENDENCE

"The parties agree that 5% of the physical value of the property of the Cities Service Gas Company, except Accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387

and 1388, should be used in estimating the value of engineering and superintendence. The Commission used 5% in its calculation and no contention exists as to this item except if any change is made in the valuation as found by the Commission as to accounts other than those herein recited this account should be adjusted accordingly.

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"Taxes During Construction

"The Commission's allowance of $778,044.00 for this account is accepted by the parties.

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"Cost of Financing

"Hamilton included in his valuation $3,422,512.00 for this item, that figure being based on 4% of the total value of the property including interest during construction and that, in his opinion, the expense was an actual one bound to occur in the reproduction of the property. Black testified that, in his opinion, the allowance was improper and did not include it in his valuation. The Commission disallowed the item in its entirety.

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"Working Capital

"The allowance of $775,000.00 made by the Commission is accepted by the parties.

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"Material and Supplies

"Hamilton testified that materials and supplies on hand September 1, 1931, according to the books of the company, amounted to $548,096.00. Black testified that he took the average cost of materials and supplies on hand June and September 1, 1931, of $509,400.00, as shown by the books of the company.

[fol. 446] "The difference between the materials and supplies on hand September 1, 1931, and an average of such supplies as of June 1 and September 1, 1931, is $57,496.00.

"Miscellaneous Construction Expenditures

"This item is discussed by the Commission at page 84 of its opinion. For the purposes of this agreement we have included it under the subsequent heading Organization Expenses, Legal and Administration Expenses During Construction and Miscellaneous Construction Expenditures.

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"Organization Expense, Legal and Administration Expenses During Construction, Miscellaneous Construction Expenditures

"These three items are considered separately by the Commission in its opinion at pages 83 and 84. Black and Hamilton, in their respective valuations, used slightly different percentages applied to different classifications but arrived at approximately the same result and made allowances for all of the items totaling approximately 2% applied to the respective physical values found by them plus allowances for engineering and supervision. For the purpose of this case, it is agreed that 2% is a proper allowance for the several items to be applied to the total of the physical value found by the court plus its allowance for engineering and supervision."

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[fol. 447] Disputed Accounts

The following accounts are in controversy on appeal:

Account No. 1312. Production—Gas well construction.

Account No. 1313. Production—Gas well equipment.

It was agreed by the parties before the District Court that:

"Black testified to a value of $1,718,813.00 new and $1,210,-392.00 depreciated for the Account No. 1312 and $658,245.00 new and $484,514.00 depreciated for Account No. 1313. Hamilton testified to a value new of $2,022,296.00 and $1,300,-025.00 depreciated for Account No. 1312 and $917,777.00 new and $573,124.00 depreciated for Account No. 1313. These two accounts are combined in this abstract in order to get comparable figures for the reason that in the evidence testi-

mony is given as to the cost to the company of wells, including equipment.

"The Commission in its opinion reduced Black's figures for Account No. 1312, $130,363.00 new and $57,233.00 depreciated, being the value placed on gas well construction (the hole) for storage wells by Black. A storage well is one which was formerly drilled for gas and has been converted into storage use. The company has two fields which it uses for storage, one known as the Craig field and the other known as the Augusta field. The fields are used as reservoirs into which gas is injected through storage wells [fol. 448] during the summer months when the demand for gas is low, as a reserve to be used when the demand is greater. The record shows that the company after these fields had been nearly depleted, leased these lands from the owners for storage purposes at a yearly rental.

"The Commission disallowed the value of these wells insofar only as the value referred to the hole, on the ground that these wells (referring to the hole only) belong to the landowners, the lessor, and not to the company, and are simply leased to the Company for the purpose mentioned in the storage lease, and that the Company has no title to them.

"To Black's figure for Account No. 1313 the Commission added $236,373.00 new and $173,925.00 depreciated because the prices Black applied to casing and tubing in the wells was considered insufficient. The Commission finding as follows: "The testimony with respect to the allowances for casing and tubing included in this account is apparently conclusive with respect to the prices fixed by Black being insufficient, while the testimony is not conclusive that the prices used by Mr. Hamilton were representative prices as of the date of his valuation. However we have accepted his total of $853,309.00 for casing and tubing in this account, corrected for overheads included, which we believe to be excessive, and have applied instead the overheads used by Mr. Black."

"The allowance by the Commission for Account No. 1312 is $1,588,450.00 new and $1,153,157.00 depreciated. For Account No. 1313, $894,618.00 new and $658,439.00 depreciated, making a total of the two accounts of $2,483,068.00 new and $1,811,596.00 depreciated. This compares with Hamilton's [fol. 449] value for the two accounts of $2,940,073.00 new

and $1,953,149.00 depreciated, leaving a difference between the Commission's finding and the amount estimated by Hamilton of $457,005.00 new and $141,553.00 depreciated.

"In addition to the estimates of Black and Hamilton contained in their respective valuations, testimony was given by Eastman as to the actual cost to the Cities Service Gas Company of certain wells in representative fields together with testimony as to the cost of adjacent and comparable wells drilled and owned by other companies. This testimony is summarized in the following tabulation:

| | Total cost | Depth | Date drilled | Record page |
|---|---|---|---|---|
| Hobbsville Field | | | | |
| Fish No. 2 C | | | | |
| Hamilton | $27,469.00 | 2932 | Dec. 1930 | Exh. #17 |
| Black | 16,880.98 | | | 2534 |
| Actual Cost to Company | 30,075.76 | | | 2534 |
| Cost of Adjacent Wells drilled by other Companies | | | | |
| Tiger #1, Midcontinent Pet. Co. | 36,193.43 | 2934 | July 1931 | 2535 |
| Smith #1, Minnehoma O. & G. Co. | 35,014.16 | 2927 | Aug. 1930 | 2535 |
| Smith #2, Minnehoma O. & G. Co. | 31,439.63 | 2922 | Apr. 1931 | 2535 |
| Brown #1, Winona Oil Co. | 36,456.30 | 2949 | Oct. 1930 | 2535 |
| Street #1, Winona Oil Co. | 33,376.44 | 2922½ | Jan. 1931 | 2535 |
| Elias #1, Texas Co. | 30,726.44 | 2895 | Aug. 1930 | 2537 |
| Average of above six wells | 35,197.73 | 2925 | | |
| Little River Field | | | | |
| Charty No. 2 | | | | |
| Hamilton | 39,326.00 | 3128 | Sept. 1929 | Exh. #17 |
| Black | 21,280.62 | | | 2538 |
| Actual Cost to Company | 42,567.44 | | | 2538 |
| Cost of Adjacent Wells drilled by other Companies | | | | |
| Alec #3, Midcontinent Pet. Co. | 37,641.48 | 3165 | | 2538 |
| Alec #1, Carter Oil Co. | 43,493.05 | 3117 | Apr. 1929 | 2540 |
| Factor #1, Carter Oil Co. | *59,531.69 | 3090 | Apr. 1929 | 2540 |
| Gotcha #13, Gypsy Oil Co. | 43,607.15 | 3152 | June 1929 | 2540 |
| Gotcha #15, Gypsy Oil Co. | 37,506.26 | 3114 | July 1929 | 2540 |
| Janney #7, Texas Co. | 38,803.75 | 3159 | July 1929 | 2541 |
| Haney #2, Sinclair O. & G. Co. | 44,791.06 | 3126 | May 1930 | 2541 |
| Smith #6, Prairie O. & G. Co. | 31,937.93 | 3205 | Mar. 1930 | 2541 |
| Average of above eight wells | 42,164.04 | 3140 | | |

* Erroneously reported in record as $159,531.69.

[fol. 450]

| | | | | |
|---|---|---|---|---|
| Perry Field: | | | | |
| Freyler No. 1 | | | | |
| Hamilton | $45,117.00 | 3467 | Oct. 1930 | 2542 |
| Black | 24,899.88 | | | 2542 |
| Actual Cost to Company | 50,530.22 | | | 2542 |

| | | | | |
|---|---|---|---|---|
| Freyler No. 2 | | | | |
| Hamilton | 44,464.00 | 3449 | Nov. 1930 | 2587 |
| Black | 24,570.87 | ..... | ..... | 2586 |
| Actual Cost to Company | 49,248.74 | ..... | ..... | 2587 |
| Cost of Adjacent Wells Drilled by Other Companies: | | | | |
| McCormick #1—Indian Territory I. O. Co. | 53,417.00 | 3387 | ..... | 2588 |
| McCormick #2—Indian Territory I. O. Co. | 53,417.00 | 3367 | ..... | 2588 |
| Walter Meyer #1 Sinclair Oil & Gas Co. | 51,430.55 | 3421 | Oct. 1929 | 2588 |
| Walter Meyer #1 Prairie Oil & Gas Co. | 47,081.60 | 3437 | May 1929 | 2589 |
| Trussel #1 Twin City Oil Co. | 51,828.36 | 3450 | Oct. 1930 | 2589 |
| Stewart #1 Twin City Oil Co. | *39,680.15 | 3405 | Mar. 1931 | 2589 |
| Average of above six wells | 49,475.78 | 3411 | ..... | .... |

* Difference in cost of Trussel and Stewart Wells was due to use of fuel and water lines of the former well in the drilling of the later without proper distribution of charges. See Record, page 2589.

Average cost of Trussel & Stewart, 45,754.26.

| | | | | |
|---|---|---|---|---|
| Amarillo Field: | | | | |
| Fuqua No. 2 | | | | |
| Hamilton | 24,981.00 | 2736 | ..... | 2595 |
| Black | 19,843.34 | ..... | ..... | 2590 |
| Actual Cost to Company | 30,197.13 | ..... | ..... | 2590 |

"In addition to estimates of Black and Hamilton and testimony by Mr. Eastman, Mr. Richie, production manager for the Derby Oil Company and theretofore production and pipe superintendent of the Marland Oil Company, having had fourteen years' experience in drilling and contracting wells in Kansas, Oklahoma, Texas, New Mexico and California, testified that he was familiar with costs of drilling wells in the Amarillo Proven Sweet Gas fields in September, 1931; that by use of rotary tools, wells could be drilled in this field at this time at a less cost than if standard tools were used, and that the Fuqua Well No. 2 and the Burnett Well No. 14, concerning the former of which respondent introduced testimony as to their actual cost, could be completed at which is [fol. 451] known as turn-key job prices as follows: The Fuqua Well No. 2 at $22,303.00 with standard and $22,101.00 with rotary tools; and that the Burnett well No. 14 could be completed for $27,301.00 with standard and $23,779.00 with rotary tools. Mr. Black's complete costs on these two wells are as follows: Fuqua well No. 2, $19,843.00 and Burnett well No. 14, $30,024.00 and total considerably more than Mr. Richie testified it would actually cost to complete these wells.

"In addition Mr. Richie stated that if he had twenty wells to drill his cost would be reduced five per cent.

"A comparison of Mr. Black's, Mr. Hamilton's and Mr. Richie's valuation of certain wells, completely equipped, is found on transcript page 2891, and follows herewith:

| Well | Black | Hamilton | Richie Standard rig | Richie Rotary |
|---|---|---|---|---|
| Fuqua No. 2 | $19,843 | $24,991 | $22,303 | $22,101 |
| Burnett No. 14 | 30,024 | 32,847 | 27,301 | 23,779." |

Eastman testified for the Company in substance as follows:

Gas well construction includes drilling of gas wells, that is, the cost of the hole; exclusive of cost of material.

Burnett Well, No. 13, shows depth of well to be 3,180 feet. The cost per foot to be $6.57; contractors price for drilling per foot, $3.50; to that is added $3.07 to cover company labor and incidental expenses making total unit cost per foot of $6.57.

Witness had no detailed items of company labor, just divided $759.00 by the average depth of the wells drilled during the period from 1925 to 1931 in that field, making 28 cents per foot. The Burnett well was drilled in 1925. [fol. 452] The contract price for drilling a well in 1929 as compared with 1931 was higher. Did not know how much, but had in mind 25 to 30 percent at the time; $3.50 per foot is the common ordinary price for drilling a well in the Aramillo field in 1931. Approximately $1.75 of the unit price is made up of what is termed incidental expenses of the company and contractor. He could not give individual items which go to make it up. One item is $1.04 payment per day for cleaning and rigging up the well after it is drilled. The above is the average unit cost price of twenty-three wells in the Amarillo field.

Eastman testified that he had made a study of the actual cost of wells drilled by the Cities Service Gas Company for the purpose of comparing such actual costs with the estimates of Hamilton and himself as contained in their valuation and the estimates of Black as contained in his valuation.

That on page 349 of Black's valuation he shows the T Buck No. 1 well in Hughes County, Texas, in which the company has a 50% interest as $6,289.00 for the half interest or $12,578.00 for the well; that he has letters from drilling contractors showing the cost of drilling quoted

at $5.00 and $5.50 per foot for drilling only exclusive of fuel, water, day labor and all incidental expense; the depth of that well is 2,481 feet; that taking $5.00 a foot, the lowest cost quoted for drilling, the drilling cost of the well would be $14,905.00. To that figure would have to be added all day labor, fuel, water and other incidentals; that the figure used by Hamilton and Eastman in their value for this well is $24,991.00, practically double the figure used by Black; that the bare drilling cost alone is in excess of the total cost allowed by Black.

That Black has included for Fish No. 4 well $12,921.00; that drilling quotations from contractors are $5.00 and [illegible] $5.50 per foot; that the depth of the well is 2,932 feet; that the drilling of this well at $5.00 per foot would cost $14,460.00 as against the figure of $12,921.00 allowed by Black for all expense. The witness introduced in evidence a photostatic copy of the job order of the company covering this well which shows the total cost of the well to the company to be $30,073.76. This figure is comparable to Black's total figure for labor and material of $16,000.91. The well was drilled in December, 1930. In this connection the witness introduced a letter from the Mid Continent Petroleum Company showing the cost of their wells known as Louisa Tiger No. 1 and George Aloe No. 3 in the same locality. The Tiger well is close to the Fish well, was drilled July 2, 1931, the total cost was $30,193.43 and the depth of the well 2,934 feet or two feet deeper than Fish No. 2. The witness also produced a letter from the Minnehoma Oil & Gas Company showing the cost of drilling their Smith No. 1 and No. 2 wells. The cost of Smith No. 1 well was $35,014.16 and the depth 2,927 feet. Smith No. 2 is 2,922 feet deep and the cost is $31,439.63. Smith No. 1 was drilled August, 1930, and Smith No. 2 April, 1931. The witness also produced a letter from the Winona Oil Company showing the cost of Jenny Brown No. 1 and Street No. 1 in the same field drilled within the last fifteen months. Brown No. 1 cost $36,456.30 and was drilled in October, 1930, to a depth of 2,949 feet. Street No. 1 cost $33,376.44, was drilled in January, 1931, to a depth of 2,922½ feet. The witness also produced a letter from the Texas Company showing cost of drilling their Burkholder No. 7, Eliza No. 1 and Janney No. 7 wells. Only one of these wells was in the same field—

Ellen No. 1, drilled in August, 1930, to a depth of 2,895 feet at a total cost of $30,726.44; that the witness went to these other companies for the purpose of finding out how their experience tallied with the experience of the Ellis Service Gas Company.

[fol. 454] Charty Well No. 2 is included in Black's valuation, page 349, at a total cost of $21,200.02, his figure for drilling, fuel, water and incidental expense being $15,416.00 and his equipment $5,784.02. This well is in the Little River Field in the Seminole area. The witness had quotations from four contractors in the Little River Field, the minimum bid for drilling being $5.00 per foot as of September 1, 1931, and the high bid of $6.50. The drilling alone for this well, figured at $5.00 per foot, would be $15,040.00 which is in excess of the figure used by Black for the completed well (exclusive of equipment). The witness produced photostatic copies of the records of the company showing actual cost of drilling and equipping Charty Well No. 2, which was introduced as Exhibit 67. The actual cost of this well, as shown by the records, was $42,507.00 or $20,000.00 in excess of the figure used by Black. For the purpose of comparison, the witness procured information from the Mid Continent Petroleum Corporation as to the cost of its Alec No. 3 in the same field. The well was drilled to a depth of 3,165 feet and cost $37,641.48. The Carter Oil Company's well, Alec No. 1, cost $43,493.05 and was drilled to a depth of 3,117 feet. The T. Proctor No. 1 well of the same company was drilled to a total depth of 3,080 feet and the cost was $159,531.62. The witness also produced a letter from the Gypsy Oil Company reporting the cost to it of two wells in the same field. M. Cotcha Well No. 13 cost $43,607.15 and was drilled to a depth of 3,152 feet. The Cotcha Well No. 15 cost $37,506.26 and was drilled to a depth of 3,114 feet. These wells were drilled in June and July of 1929. The Janney Well No. 7 of the Texas Company in the same field was drilled in July, 1929, to a depth of 3,170 feet and cost $38,803.75. The witness also produced a letter from the Sinclair Oil & Gas Company reporting the cost of drilling its Haney No. 2 well in the same field to be $44,791.16, the well being drilled in May, 1929, to a depth of 3,126 [fol. 455] feet. A letter from the Prairie Oil & Gas Company reported the cost of drilling its Bert Smith No. 6

well drilled in March, 1930, to a depth of 3,205 feet, to cost $31,937.93.

At page 350 of Black's valuation he lists the Freyler Wells Nos. 1 and 2; he gives the cost of these wells, exclusive of equipment, at $17,630.00 for No. 1, with $7,269.88 for equipment, making a total of $24,899.88. The lowest quotation from drilling contractors for drilling in this field is $5.50 per foot. The depth of Freyler No. 1 is 3,467 feet and the drilling alone would cost $19,068.50 as compared with Black's $17,630.00. A photostatic copy of the company's record showing the actual cost of this well was introduced in evidence showing the cost to be $50,530.29 as compared with Black's figure of $24,899.88 more than double the amount allowed by Black.

Eastman further testified that in preparing the unit costs which were used by Hamilton and himself in Hamilton's valuation he studied and analyzed the actual cost of the company in drilling wells in the several fields and by dividing such actual costs into the number of feet drilled arrived at a unit cost per foot which was adjusted for material and labor to present prices and then applied to the several wells.

The cost figures of the company quoted by Eastman include New York engineering overheads, right of way and miscellaneous expenses. Black included engineering and miscellaneous expense as separate items in his general overhead, and right of way in Account No. 1307.

Black testified for the Commission that the cost of drilling the Fuqua Well No. 2 as estimated by him, to be $14,834.00. That is, $4.00 is the drilling price; day work is allowed for in the total price as follows: 3 days at $80.00 per day; for fuel and water for drilling 45 days at $35.00 [fol. 4567] per day; depreciation of casing withdrawn and used $1,650.00; transportation of casing and tubing $200.00; superintendence for 45 days at $5.00, making the total of $14,834.00. The $4.00 just covers the drilling of the hole and placing the casing, etc.

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A. S. Richis, of Wichita, Kansas, witness for the Commission, testified in substance as follows:

At the present time he is Vice-President of the Derby Oil Company in charge of production and pipe lines, which

Company is engaged in the business of production of oil, refining and marketing of same, also in the production of natural gas for sale purposes. He is familiar with the business and has been for fourteen years. For ten and one half years, he was employed by the Marland Oil Company in the production division in the states of Kansas, Oklahoma, Texas, New Mexico and California. He is familiar with the Amarillo gas field, had supervision of the development in that field from the general office in Ponca City, but was not actually on the ground all the time; that he is familiar with the cost of drilling gas wells in Carson County in the Amarillo field as of September, 1931. He has made calculations of actual cost of drilling Fuqua No. 2 well in Carson County. He has made an estimate of the cost of drilling and equipping, furnishing the drilling equipment, labor, water and fuel, and turning said well over as a complete turn key job as of the date of November, 1931.

"The first item is the rig, $3,250.00, tanning, labor and construction of ponds $950.00, that makes a total of $4,200.00 for the rig, you understand this is a regulation, standard job. I have made this estimate on casing at 122 feet of 20 inch, 90 pound, $5.75 a foot, $736.00; 244 feet of 15½ inch, 70 pound, at $4.50 a foot, $1,098.00; 2,251 feet of 8¼ inch, 32 pound at $1.50, $3,445.50. I have included 2,700 feet of 2 inch, 4½ pound tubing at 22 cents, welding on the above casing depreciation on the above [fol. 457] casing $594.00, for the tubing, the welding on the casing including tubing $250.00, fuel 42 days at $15.00 per day, $630.00; water, ten dollars per day for 42 days, $420.00; 2,736 feet of hole at $3.50 per foot, $9,576.00; five days of 24 hours each day work at $80.00 per day, $400.00; miscellaneous tanks, pipe fittings and supplies, a figure of $600.00; well connections for shutting in after completion, $470.00; fence for enclosing well after completion, $58.00; miscellaneous labor and hauling, teaming that has to be done around during the work, estimated figure of $600.00; $150.00 overhead; a gross figure of $25,[illegible]. From that I have deducted the following items as salvage of rig, material only, removed from the property, with credit of $2,437.50, on your item of miscellaneous [illegible]

pipe fittings, etc., $300.00, total salvage $2,737.50, leaving a net after salvage of $22,303.50. That is estimated with standard cable tools.

"I would drill this well with rotary tools and have made an estimate of the cost of drilling this well with rotary tools, which is as follows:

"Rig material $3,500.00; pond, labor and trucking, $1,050.00; 244 feet of 12½ inch casing, $610.00; same valuation per foot as on the other, 2,297 feet of 8¼ casing, $2,445.50; 2,700 feet of two inch tubing, 4½ pound tubing, $594.00; welding on the above casing including the tubing $125.00; fuel, 20 days at $30.00 per day, $600.00; another item of fuel there of five days at $15.00 per day, for a total of $75.00; water, 20 days at $50.00 per day, $1,000.00; another item on water, five days at $10.00 per day, $50.00; contract 2,736 feet at $4.25 a foot, $11,628.00; three days day work, 24 hours each at $90.00, $270.00; miscellaneous tanks, fittings and connections and supplies $700.00; well connections $470.00; fence $58.00; cement and cementing, that is the cement and cost of cementing, $400.00; miscellaneous labor $300.00; overhead $150.00; for a gross of $25,025.50; [fol. 458] your salvage column, a figure of $2,625.00 for the rig, in your item of miscellaneous tanks, fittings and supplies, salvage of $300.00, or a total of $2,925.00 salvage, making a net for the job, after salvage of $22,100.50.

"That the cost of the rotary method would be $22,100.50, with the standard tools, $27,302.50. That he has also made calculations of a turn-key job for the full completion of the Burnett Well, No. 14, which is as follows:

"Rig material $3,250.00; labor, ponds, teaming, and trucking $950.00; casing, 260 feet of 20 inch, 90 pound, $1,495.00; 648 feet of 15½ inch, 70 pound, $2,916.00; 1115 feet of 12½ inch 50 pound, $2,787.50; 2,150 feet of 10 inch, 40 pound, $4,300.00; hauling on the above $250.00; fuel, 45 days at $15.00 per day, $675.00; water 10 dollars per day, 45 days, $450.00; contract 3,052 feet at $3.50 per foot, $10,682.00; five days of 24 hours each day work, $90.00 per day, $450.00; miscellaneous tanks, pipe and fittings and supplies, $600.00; well connections $425.00; fence $58.00; miscellaneous labor and teaming $600.00; overhead $150.00; a total of $30,038.50. From that, salvage rig only, $2,437.50; miscellaneous pipe and fittings $300.00; total salvage $2,737.50; net $27,301.00.

"That he has also made calculations of drilling of the same well equipped the same way and drilled with rotary, which is as follows:

"Rig material $3,500.00; pond, labor and trucking $1,050.00; casing 260 feet 12½ inch, $650.00; 2,400 feet 8¼ inch, $3,600.00; hauling on the above $150.00, on the above casing only, fuel 25 days at $30.00 per day, $750.00, five days at $15.00, another additional fuel item, five days at $15.00 a day, $75.00; water 25 days at $50.00, $1,250.00; additional five days of water at $15.00 per day, $75.00; contract 3,052 feet at $4.25 a foot, $12,791.00; 5 days at $90.00 [fol. 459] per day day work $450.00; miscellaneous tank fittings and supplies, $700.00, well connections $425.00; fence $58.00; cement and cementing $500.00; miscellaneous labor $350.00; overhead $150.00; total $26,704.00; salvage, rig material $2,625.00; on that item miscellaneous fittings, tanks, and supplies, $300.00; total salvage $2,925.00; making net $23,779.00.

"The cost of the above well, standard tools, is a net figure of $27,301.00, with rotary tools $23,779.00. The above cost is a fair and reasonable cost of these wells drilled in September of last year, and, in my opinion, could be drilled for that cost.

"That if he had as many as twenty wells to drill in Carson County, it could be done pretty close to 5% cheaper on the cost of the well.

"The figures on Fuqua No. 2 of Black & Veatch, the Cities Service and Richie are as follows:

"Black and Veatch cost $19,843.00, Hamilton cost $24,991.00, Richie's cost on standard tools $22,302.50, with rotary $22,100.50; Burnett No. 14, actual cost of the well as claimed by Cities Service, $30,197.13, Burnett No. 14, Black and Veatch cost $30,024.00, Hamilton cost $32,847.00, Richie, standard tools $27,301.00, with the rotary $23,779.00, the actual cost as shown by the exhibit $35,624.29.

"That the cost of drilling gas wells in the Amarillo field in September, 1931, was less than it was in 1928 and 1929."

The witness, Richie, testified on cross-examination that in making his estimates he used casing and tubing and not line pipe.

In calculating the price of new materials, it is calculated on the price at the local supply house and not at the mills.

Frequently, the estimated price of the cost of building a well varies several thousand dollars on the completed well. [fol. 460] If the cost of a well exceeded the estimate made, I would say there were some contingencies that I had not taken into consideration.

On redirect examination, the witness stated that he deemed the estimate made by him sufficiently high to take care of the average contingencies.

That he is in the contracting business and would be willing to drill the wells at the prices above testified to and to make it a turn-key job. That sometimes a well costs less than the estimate.

On re-cross examination, he stated he had provided for contractor's profit in the estimate made in the item of 2,736 feet at $3.50 per foot. General experience has taught him to make his bids a little bit over his estimate. That his estimate is a little bit high in this case. If this well did cost $30,000.00, he would still say that his judgment was probably right and that the employes did not follow instructions.

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[fol. 461] Account No. 1314. Production—Field-line equipment:

It was agreed by the parties before the District Court that:

"This account covers the labor and material necessary to construct and test pipe lines between the wells and transmission system. The account is valued by Black at $3,548,102.00 new and $3,126,159.00 depreciated. Hamilton valued the account at $4,447,806.00 new and $4,169,763.00 depreciated, the difference between the two engineers being $899,704.00 new and $1,043,604.00 depreciated.

"In pricing this account, Black testified that all field lines in Texas up to and including 4-inch were priced on the assumption that they were buried at one-half the depth of the main line and that in other states field lines up to and including 12¾ inch were assumed as being placed in trenches one-half the depth of the main line of the same size, and that ditching and backfilling was included on the basis of half depth on all lines in consideration of the fact

that approximately 872,000 feet of field lines are above the ground."

"Eastman testified that in his valuation of this account field lines above ground and those buried were separated, and the unit costs applicable were used.

"The commission found the value of this account to be $3,126,159.00, being the exact figure testified to by Black.

"The commission stated in its opinion that any necessary adjustments as to cost of pipe would be considered in connection with Account No. 1333, and such adjustment was made by adding to Account No. 1333, the amount of $544,552.00, plus $19,059.00 for overheads, for pipe in Accounts 1314 and 1333. An additional amount of $82,976.00 for pipe paint was added in Account 1333, making the total of that Account, new, including additions for pipe in Account 1314, $43,746,298.00, as noted in the opinion."

[fol. 462] Black testified for the Commission that in the Texas field he applied one-half the depth of the main line to the gathering lines, four inches and under in size. All sizes above that were taken at the same depth as lines anywhere in the main system, and have applied no place in the system half the depth to the field line greater than 10¾-inch. So far as the Texas field is concerned, the amount allowed for installation is exactly the same as we have allowed anywhere on the main line system. Half the depth of the main line was applied in Texas on 4-inch pipe or smaller. To the field lines in other states we have used half the depth of main lines up to 10¾ outside diameter. We have not figured a 16-inch pipe line in half the depth of the main line ditch, but have given it full depth. My exhibit shows some 3-inch line with 24-inch cover, also some with 22-inch cover, 4-inch line with 15-inch cover, some with 24-inch, 26-inch, 20-inch and some with 18-inch cover; that he used the same depth of ditch in the Texas field as was used by the company's engineers; that fifty per cent of the main line cost was applied only to the small size of pipe in Texas; that is partly an assumption and partly because of the fact that in this system in field lines, maybe some main lines, we have approximately 900,000 feet of pipe above ground to which we have given the depth of the ditch, cover, and et cetra; that applied in that particular classification he thinks that the fifty per cent allowance is absolutely fair and perhaps in excess of the actual conditions if thorough

inspections were made of the depth of those lines; I have covered a good many of the lines in Texas and it is all a matter of whether it averages or not by any system of inspection. It depends on whether you make enough inspections to make the average. Those costs of field line trenches are figured as having been dug with a ditching machine. I am referring to one half of the excavation and one half of the back filling which is only a certain per cent of the entire cost of laying the line. I do not mean that we [fol. 463] actually complete the operations of pipe laying, ditching and backfilling, at extra for half the price on a 4 inch field line, that we do on a 4 inch main line. Our fifty per cent figure is only on the item of excavation and back filling. For example on a 4½ inch, 10.79 lb pipe of which we have some in the Amarillo field, the unit cost of that pipe complete, that is, the labor in the main line would be $0.0316 and on a field line would be 29¢, or there is a difference of 3 cents per foot, or ten per cent.

I have my breakdown from my unit cost of ditching as follows:

One foreman at $7.00, one gang mechanic at $6.00, one timekeeper at $5.00, sixteen laborers at $3.20, or a total of $81.20, one medium sized truck and driver at $25.00, two light automobiles at $6.00 each, three teams with drivers at $6.00 each, two ditching machines with operators at $30.00 each, or a total of $224.20, plus 22% structural overhead or $49.32, or a total of $273.52, plus an allowance of $10.00 for planking and bridging material, or a total of $283.52 for a day's run of the gang of 850 yards, or a cost price of $0.333 per yard, and I have used $0.35.

On backfilling, I used one foreman at $4.50, one backfiller operator's helper $4.50, eight laborers at $3.20 each, one backfiller and operator at $22.50, or a total of $57.10. Add structural overhead of 22% or $12.56 making a total of $69.66 for a day in which this crew handled 900 cubic yards at a cost of $0.0774 for which I used $0.08.

In figuring structural overhead, I have considered the variation in workmen's compensation and public liability rates in the various states and have arrived at totals for said overheads as follows:

Texas, 23.46%; Oklahoma, 19.914%; Nebraska, 21.894%; Missouri, 21.414%; Kansas, 19.330%, and have arrived at the average figure of 22%.

[fol. 464] For the unit cost on labor on plain end 12¾ inch pipe, I have one foreman at $9.00, one at $8.00, one at $6.00, pipe stabber at $8.00, gang mechanic at $6.00, forty laborers at $128.00, timekeeper at $5.00, heavy truck and driver at $15.00, two light automobiles at $44.00, three teams and drivers at $18.00, one tractor and operator at $17.50, or a total of $264.50, to which has been added structural overhead in the amount of $58.19, making a total of $322.69. The percentage of overhead was 22%.

Eastman testified that in valuing this account an inventory was made of all field lines showing those above ground and those buried, and as to those buried the depth of the trench. This inventory shows that 12% of the field lines were above ground and 88% buried.

Eastman further testified that the unit costs used in the valuation of this account were prepared from studies made of the actual experience of the Cities Service Gas Company in constructing field lines utilizing 20,000 tons of pipe.

A. D. Bechtel, testified for the Company in substance as follows:

I live in Oakland, California, and am President of the Bechtel Kaiser Company, Ltd., Vice President of W. A. Bechtel Company, member of the executive committee of Six Companies, Inc., Vice President of Bechtel, Kaiser Rock Company, director of Bechtel Kaiser Warren Company, and partner in Bechtel Brothers. Bechtel, Kaiser, Ltd. is the only one of the above companies that does pipe line construction. They have been in the business about three years and in the last three years have built 65 miles of 20, 16 and 12 inch for the Montana Power Company, 200 miles of 18, 16 and 12¾ inch, 8, 6 and 4 inch for the Western Gas Company, 110 miles for the Texhoma Natural Gas Company of 24 and 12 inch, 140 miles for the Panhandle Construction Corporation 24 and 12 inch, 60 miles for the Stumpne Company 20 and 26 inch, 56 miles for the Pacific Coast Electric Company of 20 inch. My bids on these jobs [fol. 465] did not include materials that became an integral part of the line. Just such materials, supplies and equipment as was necessary to construction or laying the line.

I allowed in those contracts from 15 to 30 percent for contractor's profit depending on the size and type of line. I never allowed as low as 10% and am of the opinion that I could not stay in business in competitive bidding on 10% profit. There is no definite graduation in the percentage of profit. It depends on the size and type of line, involving different degrees of management, allocation of management time, etc.

I am familiar with field lines in connection with a gas system as distinguished from main transportation lines. I would say that the laying of a field line would cost more than to lay a main line.

On cross examination the witness, Bechtel, further testified:

"Q. I would like to know what you had in mind when you said it cost more to lay a field line?

A. I had in mind the particular contract we had, a given contract for the Texhoma Natural Gas Company which constituted approximately 110 miles of 12¾ and 24 inch, in Texas, which constituted the stem across the what might be termed the foot of the Panhandle line, Texas to Chicago."

It would probably be termed a trunk line. That is the only definite contract we have had that might be definitely called that.

From my experience in the one contract, the Texhoma line, I am of the opinion it costs more to lay a field line than a main line of the same size. From my observation, it is my personal opinion that field lines as shown by that contract contain more side or smaller connections coming into it, also considerable additional percentage or volume per mile of drips and other appurtenances which interfere with the cost. Also that usually the quantities which are [fol. 466] involved are smaller than on a main line job. (Tr. 2280.) In other words, it is the drips, fittings, connections and other appurtenances that make the differences, which are more than on a main line. In addition to the extra appurtenances above enumerated, there should be added the extra time it takes to do the work by the gang in attaching them.

E. McDonald Biddison testified for the Company as follows:

That he had been connected with the management both during construction and operation of gas concerns both in the Midcontinent field, Pennsylvania, West Virginia and Ohio over a period of 25 years, and has layed both main and field lines.

I call a field line a gathering line or a gathering line a field line, the connection from the wells to a central point in the field. The field line would usually cost more than for the same length and size of main line because of a greater difference in construction due to obstructions, usually less advantageous territory in which to lay the lines, cross connections to be made, further more in the construction of field lines, usually short sections are laid at a time. The expense of an organization moving into these short jobs is about the same as the expense would be to move a gang in to do a long job. Often the jobs are too short to justify the bringing of a ditching machine. In fact, field lines seldom justify the use of a ditching machine up to a pipe over 10 inches in diameter. My connection with such lines has been that of supervising, designing and inspecting, have also had charge of operation of pipe lines.

The witness, Biddison, further testified on cross examination that there is no maximum size of line that would be classified as a field line or a main line, but it depends upon the purpose to which it is put. There could be a 24 inch field line. Field lines are generally smaller. However, in some fields they may be as large as the main line. Gen- [fol. 407] erally, field lines are buried as deep as main lines and I have seen some gathering lines layed on top of the ground. The Cities Service Company have some, have seen them quite often. If layed on top of the ground, they would not be as expensive as if they are buried in a ditch or trench.

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T. R. Jones, of Dallas, Texas, testified for the company as follows:

That he was a pipeline contractor connected with the Oklahoma Contracting Company, a corporation, and is president of the same; been engaged in the pipeline contracting business for fourteen years, during that time has layed

9,000 miles of pipeline; in the year 1930 layed a double ten inch line from Jenks, Oklahoma to St. Louis, Missouri for the Ajax Pipe Line Company. The length of it was 400 miles. Also layed a 22 inch line for the Southern Natural Gas Company in Mississippi and Alabama, the length being approximately 300 miles. In the year 1929, also laid several thousand miles of the Lone Star Natural Gas Company line of all sizes from 4 inch up to 20 inch; have also laid several lines for the Cities Service Gas Company, being some of the lines involves in this controversy, such as the 20 inch line from Wichita to Ottawa, Kansas; have laid about 100 miles of the Continental 24 inch line from Texas to Chicago. The aggregate amount of money involved in the above contracts was around $20,000,000.00, that is, for labor; is familiar with pipe line systems generally, both as to main and field lines, most of the work being main line work, but has worked on some field and gathering lines. It costs more to lay field lines than main lines; that 20% is the amount used for contractor's profit; a job is figured by the actual labor cost multiplied by two and add 20% for profit; that usually brings it within the range of competitors. The witness Jones further testified on cross examination that, in his opinion, contractors can not operate on a 10% basis and remain in business.

[fol 468] Ross M. Stuart testified for the Company as follows:

I have had pipe line experience since 1905, am familiar with field lines as distinguished from main transportation lines, am familiar with the cost of ditching and backfilling of field lines as compared with main lines. It almost always costs more to put in a field line of a given size than a main line of the same size. Field lines are usually small jobs. In laying them it is often necessary to go around rigs, tanks, houses and camps, which makes the expense greater. Also they have more connections, taps, drips, gates and that sort of stuff in field lines than in main lines. It is generally understood in the industry that field lines cost more than main lines.

Ten to 15 per cent of the Company's field lines in Kansas and Oklahoma would be laid by ditching machines. In

Texas, perhaps 60% of the field lines would be laid by ditching machines. Ditching that is fit and proper to be done by machines is cheaper than by hand.

The witness, Stuntz, further testified on cross-examination:

Field lines are laid practically at the same depth as main lines. Some of the Company's lines are laid on top of the ground but very few are thus laid. There are some in Labette County and also in Pawnee County. It would be cheaper to lay the pipe on top of the ground.

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Account No. 1325. Transmission Land:

It was agreed by the parties before the District Court that:

"Black valued this account at $149,202.00 included in which were compressor station sites at Hogshooter and Owasso valued by Black at $2,000.00 and $2,000.00 respectively. The Commission deducted both the latter amounts and found a value for the account of $145,202.00. If the Hogshooter station site should not have been eliminated [fol. 469] there should be added $2,000.00 to the value found. The stipulation as to the evidence pertaining to the Hogshooter station is condensed under Account No. 1328."

Accounts Nos. 1307 and 1327. Production Rights of Way. Transmission Rights of Way:

The following agreed statement and testimony is a condensed statement of the evidence introduced on these accounts.

"These two accounts cover rights of way for production and transmission lines and telephone lines used in connection therewith and are being considered together for the reason that some controversy has arisen as to how the respective engineers classify particular lines as between production and transmission.

"Combining the two accounts Black allowed $1,208,564.00 for both cost of reproduction new and depreciated and Hamilton allowed $3,696,804.00 for both cost of reproduction new and depreciated, the difference between the two engineers

being $2,488,240.00. The Commission allowed for both accounts $1,713,512.00 or $1,983,292.00 less than Hamilton.

"There are in the system 65,440 rods of telephone right of way which Black priced at 25 cents per rod and Hamilton at 15 cents and 20 cents per rod. There is included in Black's valuation $16,360.00 for telephone right of way and Hamilton's valuation $12,475.00.

"As to the number of rods of pipe line right of way involved in the two accounts Black testified to 1,212,251 and Hamilton testified to 1,180,102. Black computed his rodage from maps furnished by the respondents which, in error, did not show certain lines which had been reclaimed and abandoned and the rodage as testified to by Hamilton is correct.

"As to the unit cost per rod to be applied to the number of rods in the system Black testified that he had never purchased any right of way and that the figures used by him were the result of information procured by his organization from other pipe line companies operating similar lines.
[fol. 470] "Eastman, testifying as to Hamilton's valuation, testified that the figures used by him were the result of studies of the actual experience of the Cities Service Gas Company in the purchase of right of way in the territory under consideration, by studies of the experience of the Continental Construction Corporation in connection with its recently built line from the Amarillo Field to Chicago, but he furnished no data as to the experience of any of these companies.

"Black testified that the unit costs developed by him were 85c per rod on pipe lines under 16-inch and $1.20 per rod for lines of 16-inch and over, made up as follows:

| | |
|---|---|
| Cost of right of way | 50¢ per rod |
| Damages and fencing for lines under 16" | 20¢ per rod |
| Damages and fencing for lines of 16" and over | 45¢ per rod |
| Cost of securing right of way for lines under 16" | 15¢ per rod |
| Cost of securing right of way for lines 16" and over | 24¢ per rod |

"Black testified that he computed the cost of securing all the right of way involved with the inclusion of an allowance for transportation, legal, and miscellaneous expenses, and arrived at a total cost of $202,000.00; that in round numbers

there were 3,000 miles of right of way which divided into the figure of $202,000.00 resulted in a figure of 21¢ per rod for cost of securing right of way; that he considered an allowance of 15¢ per rod for securing right of way on lines under 16-inch and 25¢ per rod on larger lines; that an average total cost for all right of way was $0.997 per rod.

"The witness Clinton H. Montgomery, employed by and testifying for the Commission (T. 2768), stated that he had made an audit of the books of the company covering 6,215,512 feet of pipe line and that the right of way and damage costs total $407,179.82, or an average of $1.08 per rod; that the number of rods included in his audit totaled 376,698 or 31% of the total rods included in Accounts Nos. 1307 and 1327; that 171,638 rods of said total were for lines under 16 inch and 205,060 rods for lines 16 inch and over; that applying Black's allowance of 85¢ per rod for lines under 16 inch and $1.20 for lines 16 inch and over would result in a figure of [fol. 471] $391,964.00, or $15,216.00 less than the cost of right of way and damages of $407,179.82 as found by the audit.

"In his application of unit costs Eastman divided the system of the Cities Service Gas Company into nine groups. Group 1 consisted of four counties in Texas, four counties in Oklahoma and two counties in Kansas, comprising in all 84,177.9 rods, to which he applied a unit price of $2.11 per rod; group 2 consisted of one county in Nebraska and nine counties in Kansas comprising in all 90,152.6 rods, to which he applied a unit price of $2.44; group 3 consisted of five counties in Kansas comprising in all 144,168.2 rods to which he applied a unit price of $2.86; group 4 consisted of four counties in Kansas and one in Oklahoma comprising in all 170,249.2 rods, to which he applied a unit price of $3.49 per rod; group 5 consisted of twenty-two counties in Kansas, one county in Nebraska and nine counties in Missouri comprising in all 397,423.9 rods, to which he applied a unit price of $3.54 per rod; group 6 consisted of four counties in Oklahoma, two counties in Missouri and one in Kansas comprising in all 103,430.6 rods, to which he applied a unit price of $3.02; group 7 consisted of three counties in Missouri comprising in all 17,510.0 rods, to which he applied a unit price of $2.54; group 8 consisted of eight counties in Oklahoma comprising in all 103,471.8 rods, to which he applied a unit price of $3.01 per rod; group 9 consisted of six counties in

Oklahoma comprising in all 69,517.4 rods, to which he applied a unit price of $2.95 per rod.

Eastman testified the breakdown of the unit price of $3.54 applied to group 5, the largest one of the groups, was as follows:

| | |
|---|---|
| Aerial surveys | $0.10 per rd. |
| Field surveys in staking the route of the line | .19 per rd. |
| Right of way payments for purchases of easements from land owners | 1.25 per rd. |
| Crop damage and damage to fences and trees | .70 per rd. |
| Expense of obtaining right of way agreements | .30 per rd. |
| Abstract and recording of right of way agreements | .10 per rd. |
| Miscellaneous expenses | .10 per rd. |
| Clearing, grading and fencing | .80 per rd. |
| | $3.54 per rd. |

[fol. 472] W. S. Gibson, called as a witness for respondents, testified (T. 2192-2196) that he was associated with the Prairie Pipe Line Company and had been since its organization twenty-two or twenty-three years ago, which, prior to 1915, was the Prairie Oil & Gas Company; that he has procured rights of way for that company for the past twenty-two years; that his experience has been in Arkansas, Texas, Oklahoma, Kansas, Missouri, Iowa, Illinois and Indiana; that during the time he has been associated with that company there has been purchased, under his direction, in excess of 10,000 miles of right of way; that he has been furnished with the cost analysis covering right of way used by the engineers for the respondents; that his experience has been on the basis of 8-inch lines and that he is not familiar with 16 inch or 20 inch lines; that right of way for lines in excess of 8 inch would cost more than for an 8 inch line; that on the basis of eight inch lines the cost analysis furnished by respondents appears to be about 37¢ a rod more than his experience; that included in the cost analysis furnished are two items with which he is not familiar, one being grading right of way, which, in the practice of his company, is handled under construction; that if there is eliminated from the unit cost analysis used by respondents' engineers the item of clearing and grading and

the item of aerial survey, the remaining figures are approximately correct:

"Q. In the figures used by Mr. Black he has used as the total of all items entering into right of way the sum of 85 cents for pipe 12 inch and under and $1.20 for pipe over 12 inch and up to 24. How do these figures correspond with your experience?

"A. That includes right of way damages and acquisition?

"Q. Yes, sir, right of way damages, acquisition and cost of acquiring.

"A. Well, acquisition is cost of acquiring. Why, that cannot be done. You cannot acquire it for that" (T. 2186-2187).

"B. H. Hicks, of Wichita, Kansas, testified for respondents (T. 2313-2330) that he was employed by the Cities Service Gas Company, his duties being buying pipe line right of way and settling damage claims; that he has had [fol. 4731] about four years' experience in that business; that from his experience it costs his company approximately $1.00 a rod as payment to the land owner without consideration of other elements of cost; that it is his practice in starting out to try to buy right of way for 50¢ a rod and if a farmer is encountered who will not accept 50¢ to pass him by and later come back to him; that perhaps they will have to pay such a man $230 for right of way and damages lumped together; that it is the practice and his instructions to settle all damage in advance, if possible at 50¢ per rod; that what he tries to do is purchase right of way at 50¢ per rod and settle damages for 50¢ a rod; that to start with a farmer is offered 50¢ a rod for right of way and 50¢ a rod for damages; that this is true in both Kansas and Missouri; that the average for damages per rod is about 65¢; that in states in which the Cities Service Gas Company's lines are located the average cost of acquiring right of way is 22¢; that if the owners of property are no more than 400 miles away they are interviewed personally; if they are in foreign countries negotiations are made by cable or wire; that a notary is carried along with right of way parties to take acknowledgements and is paid by the day; that the witness has nothing to do with such matters after the right of way contract is mailed to the home office and has no acquaintance with subsequent costs.

B. H. Hicks, testified:

"Q. Take the system as a whole with an average of pipe composing the main transportation lines, what has been your experience as to the cost per rod of obtaining right of way? I mean, what is your average—I will make it a little different. Divide it up. What do you have to pay a landowner on an average for right of way as of September 1, 1931?

"Q. Do you offer them 50 cents to start with for right of way and 50 cents for damages?

"A. Yes.

"Q. In what states is that true or prevalent?

"A. In Kansas, Oklahoma, Texas, Missouri and Nebraska.

"Q. There is no difference between the different states; you offer them 50 cents for right of way and 50 cents for damages the same as in Kansas and Missouri, to start out with?

"A. Yes, sir."

[fol. 474] "Q. What, in your opinion, on an average, does it cost in the states in which the Cities Service Gas Company line is located, to acquire your right of way?

"A. I would say 22 cents a rod would be very conservative."

"Q. This price you have just given, as I understand, is the same for the various states where you have purchased right of way?

"A. Practically so, yes.

"Q. What states are those?

"A. Texas, Kansas, Oklahoma, Missouri and Nebraska.

"Q. Do you find any difference in any of the states as to what these costs are, what you have stated here would be the cost in each one of the states?

"A. About a general average; yes, sir.

"Q. And be about the same in one state as it would in another?

"A. Practically."

"The Commission used the figure of $1.40 per rod which it arrived at by taking the actual average cost of right of way and damages of $1.08, as shown by the books of the

company according to an audit made by C. H. Montgomery, and adding thereto 22¢ per rod for expense of acquisition and 10¢ per rod for expense of abstracting and recording on other than telephone rights of way and allowed for the two accounts $1,713,512.00, which is an increase of $504,948.00 over the estimate made by Black but $1,983,292.00 less than the estimate of Hamilton.

"The Commission applied to the rodage in the system a price of $1.40 per rod arrived at by adopting the figure of $1.08 per rod, testified to by Montgomery in connection with his Exhibit 87, as representing the cost of right of way to the company and added thereto 22¢ per rod for expense of acquisition and 10¢ per rod for expense of abstracting and recording.

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"EASTMAN testified that Montgomery's Exhibit 87 did not represent the total cost to the company, his testimony in that regard being as follows:

"In regard to right-of-way, Mr. Eastman, as I recall the testimony, Mr. Montgomery made some studies or checked some information from the books of the company which were given to Mr. Black and used by him in figuring the unit cost which he arrived at. Do you know what those records consisted of?

"A. I presume they consisted of the job order analysis of the various lines.

[fol. 475] Mr. Welch: Do you know, Mr. Eastman?

A. Yes, sir, I do know.

Q. Do these job orders contain all of the costs, not included (included in) right-of-way?

A. No, sir, they do not.

Q. What elements are not included on the job orders?

A. The entire cost of acquiring the right-of-way, cost of abstracting, recording and a considerable portion of the right-of-way payments and damages payments are not included in this job order analysis as right of way costs.

Q. So if it should be assumed that those job order contained all the costs in connection with right-of-way, his assumption would not be correct?

A. That is not correct, no, sir.

Q. And of course, would be insufficient?

A. May I further explain why it is not correct?

Q. Certainly.

A. The work of obtaining right-of-way is carried on by the land and lease department of the several companies operated from the Bartlesville office. The salaries and expenses of these men are charged to operating expenses of the land and lease department. No attempt is made to classify these expenses by the various lines. At the end of each month, the proper portion of the expenses of this department is capitalized in a lump sum and goes into the investment records of the company as a lump sum. A considerable portion of the cost of settling damage claims and damages, for abstracting and recording, is done by the legal department. At the end of each month a proper portion of this expense of the legal department is capitalized in one lump sum, therefore, it is not possible to go back to the individual job orders and obtain all of the right-of-way costs.

Q. You would have to go to many different sources in the office to determine what these costs actually are?

A. You do, yes, sir.

Q. And did you go through all of the sources of information that you know of in arriving at the figure which you used?

A. We did • • •.

Q. I will ask you to look at Exhibit 87 just introduced by Mr. Montgomery in regard to the cost of right of way; I will ask you to state whether the cost shown on that exhibit and stated to be obtained from job orders is the entire cost in connection with that item.

A. The costs of right of way as shown on Exhibit No. 87 are not the entire costs of right of way on the various lines. As I explained some few days ago at a previous hearing, these costs include nothing for the acquisition of the right of way, which is a major item.

Q. What do you mean by cost of acquisition of right of way?

A. Going out and securing right of way, having it abstracted and recorded.

Q. That is, it does not include the expense of men in the field, the automobiles, phone calls, and all that?

A. No, sir, it does not.

[fol. 476] Q. And that, you mean, is the major item in connection with procuring right or way?

A. That is a major item.

Q. Where do those costs appear?

A. They appear eventually in the plant and investment account of the company as overhead construction costs capitalized, or I believe the caption here as shown in Mr. Montgomery's Exhibit No. 91, is 'General Construction and Investment Expenditures.' They are not reflected by individual job orders.

Q. So Exhibit 87 does not include all the costs of acquiring right of way?

A. No, sir, it does not.

Q. Have you considered all of thes matters in the unit costs you have used?

A. We have, yes.

Q. And did you arrive at these costs by studying the actual experience of the company?

A. We did, I might further say that these costs as shown in Exhibit 87 include nothing for locating right of way originally. The cost of that also enters the investment account of the company through General Construction and Investment Expenses. * * *"

"On cross-examination Mr. Eastman testified as follows:

'Q. It is possible that in this job account for the Cities Service Gas Company that the legal expense and the expense of obtaining the abstract and incidental expenses of the right of way, etc., are included right in that job account, isn't it?

'A. From the way in which this sheet is prepared it is possible, for from my knowledge of actual practice of the company I would say it does not include any of these items.

'Q. It is not true, then that always on a job order with reference to construction of pipe lines the legal expense, including expense accounts and incidental expense, telephone, etc., are carried in some other account; but it is possible they may be carried in the job account; is that right?

'A. It is possible they might be carried in the job order, yes, sir'' (Tr. 2797, 2789).

"Black has included engineering and staking out under the engineering account, No. 1390. The cost of clearing,

grading and construction damages have been included under construction cost. These items appear to be properly included in these accounts under the practice of the company. Exhibit 38 consists of one of the contracts under which the contractor agrees to perform the following services:

'It is mutually understood and agreed between the parties hereto that the prices thereinabove mentioned and set forth to be paid second party by first party includes the costs of clearing the right of way before construction and cleaning up right of way after the completion of the work and shall also cover all repairs to fences and all *all* costs [fol. 477] of other improvement damages which are to be paid by the second party hereto free of any cost, charge or expense to first party.

'Such damages for which the contractor is responsible includes repairs to fences, hedges and roads, and damage done to or by stock escaping through fences or gates left open or insecurely closed, as well as any and all damage to stock on account of being frightened, damage due to cutting hedge, damages to travelers in horse-drawn or automobive equipment, or stock caused by open ditches, and in general any damages that might have been avoided by care on the part of the contractor. All such claims for damages for which the contractor is liable shall be settled by the contractor' (Ex. 38).

"This contract also provides that the contractor is to receive construction material furnished by the company at rail points closest the work and to transport such material used in excavation and construction of the pipe line and back fill for certain stipulated prices. Grading of the rights of way, which is a construction cost, is not mentioned in the items which the company is to furnish or perform for the contractor, and is included as an item incidental to excavation.

"BLACK testified as to serial survey as follows (TR. 2063).

'Q. Aren't all the pipe lines being built now first surveyed with an aerial map?

'A. I don't think these lines were or are.

'Q. You have thrown out any aerial map because it was not used when the lines were constructed. I don't see

why you should do that and put in a ditching machine when that did not exist?

'A. I would be quite willing to include the cost of an aerial survey for the main lines of this or any other system, if the system reflects the advantages we would get from such a survey.

'Q. Well, if this system were to be built to-day, and none of it existed at all, wouldn't you start in with an aerial map?

'A. I might, but the valuation of this particular system is of this system as it now is, and the chief advantage of an aerial map is to show you how you can better your location or speed up the construction, or do a thousand and one things which have not been done in this property as it now exists.

'Q. But if we are reproducting it now, to-day, on which the theory of the valuation is, we would start in with an aerial map, wouldn't we?

'A. If you were reproducing it to-day I don't think you would build the property in the same location. You must remember that the valuation we are making is of this property in a specific location.' ''

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[fol. 478] Account No. 1328. Transmission—Compressor station structures:

The evidence pertaining to this account was submitted to the District Court on the following agreed statement and evidence:

''This account includes buildings, housing compressor stations together with dwellings, garages, machine shops, dams and other buildings used in connection therewith. It does not include the equipment or furnishings in any of these buildings.

''This account was valued by Black at $1,806,823.00 new and $1,567,605.00 depreciated. It was valued by Hamilton at $2,482,629.00 new and $2,267,443.00 depreciated. The difference between the two engineers on depreciated or present value is $699,838.00.

''The Commission found the present or depreciated value of this account to be $1,466,102.00. The difference between

the value found by Hamilton and the value found by the Commission is $801,341.00.

"Included in this account at the compressor stations at Hogshooter, Hominy and Owasso, Oklahoma, and the present value of the structures as found by Black and by Hamilton in the following tabulation:

| Structures | Black | Hamilton |
|---|---|---|
| Hogshooter Station | $49,560 | $84,999 |
| Hominy Station | 7,793 | 8,897 |
| Owasso Station | 44,150 | 55,683 |
| Total | 101,503 | 149,779 |

[fol. 479] "In arriving at its value of $1,466,102.00 the Commission accepted the present value as testified to by Black and eliminated the present value of the structures at Hogshooter, Hominy and Owasso as testified to by Black in the total sum of $101,503.00. The difference between Black and Hamilton of $699,838.00, when added to the $101,503.00 disallowed for the structures at Hogshooter, Hominy, and Owasso, makes the total of $601,341.00, which is the difference between the valuation testified to by Hamilton and the value found by the Commission.

"Black introduced in evidence, as Exhibit 53, photostatic copies of sworn tax returns of the Cities Service Gas Company to the Oklahoma Tax Commission in which reports it was stated that at the date of said returns, February 1, 1931, the Hominy compressor station was being reclaimed and that the Hogshooter compressor station 'is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000.00.'

"It is admitted that the Owasso station is not connected with any lines of the Cities Service Gas Company; that the equipment has been moved from the station and that the station is not used or useful at this time in gas operations.

"Eastman testified that the Hogshooter station was originally constructed to pump gas out of the Hogshooter Field into the Kansas Natural system; that the Hogshooter Field became exhausted and lines were extended to the South into the Owasso and Catoosa districts and the station became a main line station boosting gas from the

South and also pumping gas from the field to the west; at that time the load on the system had not assumed anything like present proportions and when the fields to the South became exhausted the Hogshooter station was used to pump gas from the Osage Fields North through the Kansas Natural System; during the last three, four or probably five years, the station had not been operated due to the fact that additional compressor station capacity was installed at the Tallant station and the main source of gas [fol. 480] supply shifted to other locations; that the lines to the Hogshooter station are coupled with old styled dresser couplings not capable of standing the high pressures under which the company now operates; that for three or four years it was thought probable the Hogshooter station would be abandoned and reclaimed and it was the intention of the company to so abandon and reclaim it but this was not done; within the last year one of the major sources of supply for the system has shifted to the Oklahoma City Field, which makes necessary a complete rearrangement of operating conditions; that the discovery of gas in the Oklahoma City Field has necessitated a complete rearrangement of operating conditions; that in order to render service on the eastern portion of the system it is now necessary to either increase the compressor station capacity at Tallant or operate the Hogshooter station; that it will probably be necessary to construct a line from the Oklahoma City Field in an easterly direction to connect with the Seminole line if the company is able to maintain a supply of gas. The Company is only refraining from operating the Hogshooter station at the present time because of the fact that before it is placed in operation, except in case of emergency, it is the desire to weld the 18-inch line extending North from the station so it will be capable of carrying high pressures; and that a requisition for that work has been prepared at the present time.

Eastman testified on direct:

'Q. In your opinion, Mr. Eastman, is that Hogshooter station at this time useful to the pipe line project of the Cities Service Gas Company?

'A. Yes, sir, it is.

'Q. And it is the bona fide intention of the company to place it in operation?

'A. That is correct. I am not positive that it is in operation today? (Tr. 2523-2529)'

[fol. 481] "On cross-examination by attorney for the Commission Eastman testified that the Hogshooter station was constructed about 1909; that an 18-inch line leads North from the station and a 16-inch line West. The station was shut down about 1924 or 1925 and has not been in active operation since that time; since that time the station has not been used for the purpose of supplying gas to the customers; the total value placed on the station by Hamilton and the Witness was $756,682.00 new and $426,792.00 depreciated; that land valued at $2,000.00 is not included in the figures given; that the figures given do not include undistributed overheads.

"As to Hominy, Eastman testified that the compressor station had been removed and that all that remained and all included in Hamilton's valuation were several cottages used by the pipe line employees, the rental of which is included in the exhibit covering income and a water pump and gas engine, the use of which the witness did not know unless it was fire protection for the cottages, but that if the pump and engine were not used and useful they would have been reclaimed.

"W. D. Truman Construction Engineer for the Kansas City Structural Steel Company, testified that he was employed by the respondents to estimate the cost of the main structures at the five compressor stations located at Higgins, Texas, Tallant and Drumright, Oklahoma, and Ottawa and Graham, Kansas; that he was familiar with the construction of structural steel buildings but not concrete foundations; that he selected George P. Reintjes, a contractor of Kansas City, Missouri, to estimate that part of the work for him; that Truman visited all compressor stations and Reintjes visited all but Higgins, and estimated in detail the cost of their reconstruction; that their estimate of the various stations, as compared with the valuation of Black, was as follows:

[fol. 482]

| Station | Black's valuation | Truman's valuation including Reintjes' estimates |
|---|---|---|
| Higgins | $38,010.00 | $64,115.00 |
| Tallant | 26,953.00 | 43,885.56 |
| Drumright | 23,610.00 | 46,679.98 |
| Ottawa | 40,232.00 | 52,677.49 |
| Grabham | 51,601.00 | 77,197.00 |
| | $180,406.00 | $284,555.03 |

"Truman further testified that he added to his figures for superstructures the figure given him by Reintjes for substructures to arrive at the total given in the above table.

"The total estimate of Truman and Reintjes divided as to the part estimated by Truman and the part estimated by Reintjes, and a comparison of Truman's and Black's estimates of superstructures for the five stations is as follows:

| Station | Truman's valuation including Reintjes' estimates | Reintjes' estimate of foundations, etc. | Truman's valuation of superstructures | Black's valuation of superstructures |
|---|---|---|---|---|
| Higgins | $64,115.00 | $45,400.00 | $18,715.00 | $18,530.11 |
| Tallant | 43,885.56 | 29,403.56 | 14,482.00 | 13,020.04 |
| Drumright | 46,679.98 | 36,313.58 | 10,366.40 | 10,858.00 |
| Ottawa | 52,677.49 | 34,924.09 | 17,753.40 | 17,784.32 |
| Grabham | 77,197.00 | 49,410.36 | 27,786.64 | 24,502.00 |
| | 284,555.03 | 195,451.59 | 89,103.44 | 84,694.47 |

"George P. Reintjes testified for respondents that he had many years' experience in the construction business and that his estimate for the foundations and substructures of the five compressor stations was correct.

"George Rinner, an experienced estimator for the Leeper Construction Company of Topeka, Kansas, testified that he had been employed by the State to estimate the foundations and substructures at the Ottawa and Grabham compressor stations estimated by Reintjes and that his estimate for the construction at Grabham was $28,434.00 as against the estimate of $45,019.00 by Reintjes and that his estimate at Ottawa was $19,048.00 as against Reintjes' estimate of $29,617.00 and that he would be willing to contract the work for 10% less than his estimates; that he had examined [fol. 483] Reintjes' quantities and prices on those stations, but had not estimated in detail, and the same proportionate difference between the Reintjes' estimates and his

own would apply to the five stations. The total of Rinner's estimate on Ottawa and Grabham was $47,482, and deducting ten per cent would be $42,734; Reintjes' estimate on the same items was $74,636 or 175 per cent of Rinner's estimate.

Rinner testified that his firm bid $12.63 per cubic yard of concrete, including reinforcing, forms contractor's profit, and all incidental items on the post office building at Topeka, and that his firm lost the work because it was not the low bidder.

Black made an analysis of Reintjes' figure on concrete construction on five stations, and stated that they averaged $29.69 per cubic yard at Ottawa, $41.03 per cubic yard at Higgins, Texas, $21.75 per cubic yard at Grabham, $19.91 at Drumright and $28.34 per cubic yard at Tallant; that on work designated in Black's office, Reintjes had made bids on concrete as follows: $13.40 per cubic yard on reinforced concrete at Evansville, Ind.; $21 a cubic yard on reinforced concrete at Fredonia, Kan.; $20 per cubic yard on reinforced concrete at Holton, Kans.; and that on all these jobs Reintjes was not the low bidder.

"Eastman, for respondent, testified that he had examined the records of the Cities Service Gas Company to determine the actual cost to it of the compressor station structures at nine stations and that the actual cost to the company was the figure appearing in the first column of the following tabulation, the second column of which shows the value found by Hamilton and the third column the value found by Black and that Black's figures for the nine sta- [fol. 484] tions would have to be increased 42% to equal the actual cost of the structures to the company.

| Station | Actual cost | Hamilton | Black |
|---|---|---|---|
| Blackwell | $41,303 | $49,401 | $41,358 |
| Corwin | 58,101 | 57,650 | 34,995 |
| Drumright | 37,045 | 42,121 | 23,610 |
| Higgins | 57,658 | 57,650 | 23,610 |
| Matfield | 52,004 | 49,550 | 34,497 |
| Moreland | 64,633 | 59,402 | 39,177 |
| Ottawa | 57,726 | 59,402 | 40,232 |
| Pampa | 64,783 | 51,228 | 34,417 |
| Wichita | 84,418 | 72,495 | 77,068 |
| Total | 517,671 | 498,899 | 363,364 |

[fol. 485] "In explaining the figure of $77,068 found by Black for the Wichita station as compared with the figure of $72,495.00 found by Hamilton, Eastman testified:

"Q. You referred a moment ago to the comparative figures at Wichita on the compressor station. Have you those figures with the foundation included?

"A. Yes, sir; the figures which I gave applying to the main building at Wichita were as follows: Actual cost $84,418, the value which we placed on the building $72,495, and the value which Mr. Black placed on the building $77,068. The Wichita compressor station is built in a plot of low ground near the city of Wichita, and on a very sandy soil. It was necessary in the construction of that station to drive an immense quantity of piling before the foundation could be laid, and the building and the engines and everything connected with the station rests on these piling. There has been a tremendous amount of filling done to bring the ground level of the station up above the water line. In making our comparison with Mr. Black's figures, we believe that he has included certain of this piling under the engines in with the cost of the building, because the figure which we have used for the building, or the value which we have placed on the building is $72,495, and Mr. Black's figure is $77,068. The value which we have placed on the engine foundations is $73,700, and Mr. Black's figure only $36,057, making a total of the two items in our valuation of $146,193, and in Mr. Black's valuation $113,125, and the piling under the engine foundations are not reflected in the cost which I have given as the actual cost of the building. One of the exhibits that we have filed contains a very good picture of this station when it was in the process of construction, and shows the piling."

"Eastman testified that he had also made an examination of the books and records of the Cities Service Gas Company for the purpose of ascertaining the actual cost to it of the auxiliary buildings and structures on the several compressor station sites and found the total actual cost to the company of main and auxiliary structures to be as set out in the first column of the following tabulation, the second column of which tabulation shows the amount included by Hamilton and the third column the amount included by Black:

| Station | Actual cost | Hamilton | Black |
|---|---|---|---|
| Corwin | $118,188 (0) | $115,763 (0) | $80,074 (0) |
| Higgins | 129,286 (0) | 122,890 (0) | 89,060 (0) |
| Mathield | 131,704 (0) | 118,281 (0) | 86,074 (0) |
| Ottawa | 112,503 (0) | 109,297 (0) | 86,469 (0) |
| Blackwell | 97,265 (0) | 95,007 (0) | 75,097 (0) |
| Drumright | 128,320 (0) | 121,000 (0) | 85,874 (0) |
| Wichita | 120,792 (0) | 105,215 (0) | 104,542 (0) |
| Moreland | 132,197 (0) | 119,402 (0) | 85,177 (0) |
| Pampa | 146,812 (0) | 119,000 (0) | 90,200 (0) |
| | $1,123,103 (0) | 1,027,757 (0) | 782,873 (0) |

"Eastman testified that the figures shown in the first column of the above tabulation were accurate and represent the actual cost to the company of all buildings and [fol. 486] structures at the several compressor stations and that Black's figure would have to be increased 45% to equal such actual cost and that Hamilton's figure would have to be increased 9.4%.

"In support of Hamilton's cost of reproduction new of structures in this account, Eastman testified that no breakdown of materials and labor prices were available and produced none; Black submitted details of both labor and materials prices. On rehearing this breakdown was submitted.

"The testimony in regard to the present or depreciated condition of this account was that of Eastman, Hamilton and Black and that of P. McDonald Biddison, a gas engineer employed by respondents for that purpose. The average per cent condition testified to by the several witnesses respectively, and used by the Commission covering all the structures in the account was as follows:

| Hamilton | Black | Biddison | Commission |
|---|---|---|---|
| 91.33 | 86.76 | 88.82 | 87.89 |

H. D. Renfrow, superintendent of compressor stations for the company introduced an exhibit on the per cent condition of the company's compressor stations as shown by his inspection, and that he reached exactly the same per cent condition as did Biddison, to-wit: 88.82 per cent, although working independently, arrived at exactly the same figure.

"The Commission used Black's percentages as to individual structures, the percentage of 87.89 as against Black's

86.76 being the result of the elimination by the Commission of the stations at Hogshooter, Hominy and Owasso, which stations, being older, carried a lower per cent condition.

"The nine stations above tabulated were built within the past four years and represent $1,027,757.00 in value as found by Hamilton out of his total value for this item of $2,482,629.00, or 41.4%. The nine stations selected were built within the past four years and are representative of the thirty-four stations comprising the account and on this basis of original cost to the company, the total account would be $2,713,909.00 or 9% in excess of Hamilton's estimate.

"The record shows that Eastman determined the per cent condition applied to respondents property rather than applying the per cent condition found by the engineers making the inspection.

"He testified as follows:

"Q. Mr. Eastman, using the method that you have here used in arriving at depreciated condition of the production field measuring station, you are asking the present customers to give you a return upon the property at a 97 per [fol. 487] cent condition, and in addition to that, an amortization figure of, what per cent was that, eight per cent?

"A. We are asking our customers to give us a fair return on the fair value of all the property. We are also asking them to provide a revenue from which we may have our property returned to us at the expiration of its useful life.

"Q. That is, you are asking them to return the property over a basis of twenty-one years, and at the same time to give you a return upon the property value at 97 per cent of its reproduction cost new?

"A. We are asking them to provide revenues which will give us a return on the fair value of our property.

"Q. At 97 per cent?

"A. Perhaps it might clarify things slightly if I——

"Commissioner Hill: Can't you answer it yes or no?

"A. Not without an explanation.

"Q. I think my question is plain enough.

"A. Of certain property, yes, sir.

"Q. This property. We are speaking of the specific property.

"A. I would like to make a further explanation of it, if I may.

"Commissioner Hill: All right.

"A. Perhaps it would clarify the situation if I would state my position, or belief, as to what should be deducted from the rate base because of accrued depreciation or physical deterioration.

"Q. I might say this, we understand what you have done, what we are asking for now is the effect of it.

"A. I am trying to tell you the reason for it.

"Q. All right, go ahead.

"A. I believe only such amounts should be deducted from reproduction costs, new, in arriving at a rate base, as is reflected in loss, primarily, of efficient operation, or only such amounts should be deducted as will be necessary to restore the property to full operating condition. That is what we have in general done here, by rating the property in a per cent corresponding to new property and should apply to all of the property with the exception of property which it is necessary to amortize, *property which it is necessary to amortize*, in general consisting of leaseholds and wells, and other production property."

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Account No. 1331. Transmission—Compressor-station equipment:

The evidence pertaining to this account was submitted to the District Court on the following agreed statement and evidence:

"This account covers all machinery and equipment used in connection with the operation of compressor stations.

"The account is valued by Black at $9,660,183.00 new and $8,482,419.0- depreciated.

"Hamilton valued the account at $9,773,788.00 new and $8,873,812.00 depreciated.

"The difference between Black and Hamilton on present or depreciated value is $391,393.00.

"The Commission found the value of the account to be $8,048,910.00.

"Black valued the equipment in the Hogshooter station at $414,925.00 depreciated and Hamilton valued the same equipment at $341,794.00.

"Black valued the equipment in the Hominy station at [fol. 488] $1,548.00 depreciated and Hamilton valued the same equipment at $1,471.00.

"Black valued the equipment at Owasso at $17,036.00 depreciated and Hamilton valued the same equipment at $14,361.00.

"On the equipment in the three stations Black was $75,943.00 higher than Hamilton on his depreciated value or 21%. The Commission eliminated from the total value of this account $433,509.00, which is Black's figure for the present value of the equipment in the Hogshooter, Hominy and Owasso stations. Hamilton's figure for the value of these stations was $75,943.00 less. but the Commission adopted Black's figure.

"If the stations at Hogshooter and Hominy should be included the Commission's value, as found for this account should be increased $416,473.00, making the total of $8,465,383.00, which is $408,429.00 less than the value as testified to by Hamilton, which is accounted for largely by the difference in per cent condition used by the respective engineers.

"No contention will be made by complainants as to this account other than that the equipment at Hogshooter and Hominy should be included in the sum of $416,473.00.

"The evidence on which these stations have been eliminated is set out under Acct. No. 1328."

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Account No. 1333. Transmission-line equipment:

It was agreed by the parties before the District Court that:

"This account covers the transmission pipe line of the Cities Service Gas Company in place including both material and labor.

"The account was valued by Hamilton at $46,893,014.00 new and $43,578,602.00 depreciated. Black valued the account at $43,099,711.00 new and $38,842,371.00 depreciated. The difference between the two engineers is $3,793,303.00 new and $4,736,231.00 depreciated. The Commission valued the account depreciated at $39,432,351.00 being an increase of $589,960.00 over the value found by Black but still $4,146,271.00 less than the amount claimed by Hamilton.

"The addition of $389,960.00 made by the Commission to the value found by Black covers pipe and paint, the

[fol. 489] Commission having found the value of the pipe in the system to be $26,931,305.00 which, for the purpose of this case, will be accepted by the parties.

"The remaining difference between the value for the entire account as found by the Commission and that as claimed by Hamilton is accounted for by the difference in per cent condition found by Black and adopted by the Commission and the per cent condition claimed by Hamilton and by the difference in estimates by Black and Hamilton as to the amount of rock excavation in the system and the price to be applied to such rock excavation."

For the purpose of this appeal the parties have agreed to accept per cent condition found by the court and the unit cost which the court found should be applied to rock excavation, leaving in dispute only the amount of rock excavation to which the agreed price should be applied.

Eastman testified that the amount of rock excavation shown by Hamilton's valuation was determined by engineers sent out over all the lines for that purpose and who procured their information from surface observations and from talking with company employees who had been in charge of maintenance work for years and from repeated excavation of the lines were familiar with soil conditions. That where shoot rock was shown in the valuation it had been calculated as solid from top to bottom of the trench, and that where pick rock was shown the entire excavation had been calculated as pick rock. That he developed a unit cost of $7.38 per cubic yard for shoot rock and $4.01 per cubic yard for pick rock.

Mr. Eastman further testified:

"* * * Q. As I understand it, there is quite a difference between your valuation and Mr. Black's covering the item of rock excavation?

A. That is correct, there is a big difference.

Q. We have covered the one line from Ottawa to Wichita, which was constructed by Mr. Jones. Leaving that out, [fol. 490] what study did you make of the balance of the system to determine the percentage of rock?

A. We did not attempt to determine rock excavation on a percentage basis. At the beginning of this work, we sent four engineering parties into the field for the purpose of

checking lines. These parties were each composed of two graduate engineers, and they went over these lines in detail, in many cases walking the length of the line, together with the district superintendent of that district, or his foreman, or the line walkers. They went over each line and every line in detail to determine the amount of rock excavation on that particular line.

Q. These lines are frequently opened in maintenance work, are they not?

A. They are, and the district superintendents and operators of these lines in the various districts, have a very good knowledge of where rock exists, by the time they have lived with these pipe lines for years, as a great many of them have, quite an intimate knowledge of soil conditions and other physical conditions in the lines in their particular districts. We took advantage of all this information.

Q. And it is your belief that your figures are correct in regard to the rock that you have shown?

A. It is my belief that our figures are quite conservative as to the matter of rock.

Q. Have you made any computation of the difference in the valuations on account of rock excavation?

A. No, sir, we have not, for the reason that we have set out lines up in a different way than Mr. Black and that computation would require considerable time and amount of work to obtain. We have made comparisons on certain lines.

Q. Did you make comparisons on certain representative lines?

A. Yes, sir.

Q. What was the result of that study?

[fol. 491] A. We have made a comparison on certain representative lines between the amounts allowed by Mr. Black for classified excavation and our own allowances for pick rock and shoot rock excavation. On the Cambridge-Petrolia line, which is a 12 inch line, Mr. Black has allowed $21,043 for classified excavation. Our comparable figure is $179,986. I might further say that this line is laid almost entirely in solid rock. On the Falls City line, Mr. Black has allowed a total of $7,153 for classified exca-

vation, our comparable figure is $17,216. On the Fort Scott 8 inch line, Mr. Black has allowed $21,871 for classified excavation, our comparable figure is $67,371. On the Kansas City No. 3 line, Mr. Black has allowed $19,325 for classified excavation, our comparable figure is $24,715. On the Ottawa-Sedalia line, Mr. Black has allowed $12,757 for classified excavation, our comparable figure is $24,606. On the Topeka 16 inch line, Mr. Black has allowed $22,381 for classified excavation, our comparable figure is $63,021. On the Pampa-Wichita line, Mr. Black has allowed $13,351 for classified excavation, our comparable figure is $101,873. On the new southern trunk, 16 inch, Mr. Black has allowed $6,397 for classified excavation, our comparable figure is $15,735.

Commissioner Hill: Is that the line from Grabham east?

A. Grabham station east, yes, sir.

Commissioner Hill: How much did you allow for rock?

A. $15,735, against $6,397 allowed by Mr. Black.

Commissioner Hill: Doesn't that go straight east?

A. Yes, sir, straight east from Grabham station.

Commissioner Hill: In Labett county?

A. I am — sure whether this section of the line extends as far as Labett County or not. It is the new portion of that line. On the Wichita-Ottawa 20 inch line, which we had under discussion some days ago, Mr. Black [fol. 492] has allowed $57,155 for classified excavation, our figure, comparable to this, is $390,275. These lines are all in the State of Kansas. In explanation of the rock in the State of Kansas, I think it might be well to point the fact that there is a great deal more rock in southern Kansas than a person ordinarily thinks about. There are several limestone ridges running in an easterly and westerly direction which cross eastern Kansas and on practically each one of these ridges is located a cement plant. Our line crosses every one of these ridges and the eastern portion of the system in a country which is not normally considered as being particularly rocky, is in fact quite rocky, where our lines traverse it. On the Ottawa-Sedalia 12 inch line, in the State of Missouri, Mr. Black has allowed for classified excavation $26,080, our comparable figure is $63,962. On the Saginaw-Springfield line, Mr. Black has allowed $32,412, our comparable figure is $195,145.

Q. A number of those lines were built quite recently, were they not, within the last one or two years?

A. Yes, sir, most of those lines were.

Q. In connection with the building of those lines, I will ask you if your department had engineers present with the contractor to make time studies of the construction as it progressed?

A. We did in a large number of cases. We did not in every case, of course, but we studied quite a number of those lines during the construction period.

Q. Those men had no data other than to observe all of the different elements entering into the construction of the line?

A. That is correct, and to keep data in that connection. [fol. 493] Q. And did you consider all that information in connection with your determination of the rock formation?

A. We have data both as to determination as to the amount of rock and the cost of rock excavation. I did not cover the lines in Oklahoma and Texas, but the differentials existing in the States of Missouri and Kansas apply in a general way to our figures and Mr. Black's in Oklahoma and Texas."

Black testified with respect to classified excavation that he determined the percentage of such excavation by observation of the territory through which the major part of the line passed and from his knowledge of the territory [fol. 494] gained through more than twenty years of experience. He testified that he made a personal inspection of line "G" from Wichita to Ottawa, that he allowed $2.50 per cubic yard for all classified excavation whether solid or loose rock and had allowed this amount in addition to ordinary cost of trenching and backfilling of ditches of the same dimensions.

Black introduced exhibit 77 which compares the contract costs of unloading pipe and materials, hauling, stringing, ditching in all classes of material, laying pipe, backfilling and testing on seven of the lines in this property, with the amounts claimed in Hamilton's exhibit for "pick rock" and "shoot rock" only. Line "G" between Wichita and Ottawa, cost the company $0.59 per foot for all the above operations, including rock excavations, under a contract

dated June 22, 1928, or a total of $379,699.00. Hamilton's valuation, based on an analysis of costs of contract operations, shows the cost of rock excavation alone to be $390,276, or $10,577 more than the contract cost of all operations for the construction of this line, excepting welding and painting.

Jones testified that he was a pipeline contractor with fourteen years' experience and had constructed pipelines involving $20,000,000 for labor; that he had contracted with the company in the construction of Line "G" between Wichita and Ottawa to unload, haul, string and lay the pipe, excavate the ditches, including shoot rock and pick rock, backfill and test the line, for 59 cents per running foot. That he received a total of $895,985.67 for this contract and that he lost $128,000 on it, but he did not allocate any part of this loss to pipe unloading, hauling, stringing, ditching, backfilling, or to the other operations for which he received unit payments in addition to the 59 cents per foot, and which amounted to $516,287 in addition to the $379,699 paid for the operations included in the 59 cents per foot bid; that the reasonable cost per lineal foot for excavating solid rock would be "a little over 75 cents" in a ditch 28 inches by 40 inches; that such a ditch contains 7.8 cubic feet of excavation per lineal foot of ditch, and the cost of solid rock excavation per cubic foot may be taken as 9.62 costs. That his testimony concerning the reasonable cost for solid rock excavation was made after the completion of this contract.

Mr. Eastman testified with reference to the actual cost to [fol. 495] the company of eleven major lines which the Cities Service Gas Company had constructed during the past three or four years, the actual cost of construction was averaged as follows:

"Q. Now, you may proceed with whatever comparisons you made?

"A. We have made a comparison of eleven major lines, comparing the actual cost of labor to the company, including those lines, with the labor costs which we have used in our valuation and with the labor costs which Mr. Black has used in his valuation. These lines have all been laid within the last three or four years, and, in some cases, within the last two years. During that period of time there has been but slight decrease in any of the labor costs, so

that the figures, we feel, are fairly comparable. The lines which we have compared vary in size from 8-inch to 20-inch. In making these comparisons, it has really been necessary to make two comparisons, because of the fact that in the setup which we have used in presenting our valuation we have included the labor of placing the couplings, together with the cost of couplings. The first line on which we have a comparison was the line known as the Hutchinson-Lyons-Superior line, extending from Hutchinson, Kansas, to Superior, Nebraska, the total cost of labor on that line, as paid by the company, was $355,893. The labor cost which we have used in our valuation is $382,744. Adding now the couplings and the labor of placing the couplings, to make the figure comparable to Mr. Black's figure, the figure which we have used becomes $429,343, as compared to Mr. Black's figure of $348,436, or a difference of some $80,000.

"Q. Now that is, comparing your valuation, these several figures with the actual experience of the company and the actual cost to it in money?

"A. That is correct. In the case of the Fort Scott line, which is a line extending from a point north of Chanute, Kansas, in an easterly direction to Fort Scott, the actual cost of the line to the company,—8-inch line—was $202,184, and it should be borne in mind these costs I am quoting are for labor only, they include no material; Hamilton's estimate for labor comparable with this is $180,961.

"Q. What is the difference between the two?

"A. Approximately $22,000—$21,000.

"Q. So your figure is $21,000 or $22,000 less than it actually cost the company?

"A. That is correct. If we add to our figure the couplings to make it comparable with Mr. Black's, our figure becomes $194,736, which compares with Mr. Black's figure of $139,639.

"Q. What is the difference there?

"A. Approximately $54,000.

"Q. So it is that much less on that line under the actual experience of the company?

"A. That is correct.

"Q. Any other lines?

"A. I have eleven of these lines analyzed, I do not know whether you desire to read all of them or not. I have not had them made up in the form of an exhibit.

"Q. Well, are they all in the record, then?

"A. In the case of the Saginaw-Springfield line, which is a line extending from a point south of Joplin, Mo., to Springfield, Mo., 10-inch line, the actual cost to the company was $380,394. Our comparable figure to this is $442,570, adding the couplings our figure becomes $489,809, as compared to Mr. Black's figure of $343,085.

"Q. What is the difference on that line?

"A. About $140,000.

"Q. That is, Mr. Black is $140,000 less than the actual cost to the company?

"A. No, not less than the actual cost to the company in this particular line, less than our figure, that is $40,000 in- [fol. 496] cluding the couplings, less than the actual cost to the company, in which figures, of course, referring to the actual cost to the company of couplings or welds, are not included.

"Q. You were high on that—on your estimate on that particular line?

"A. Yes, sir, we were high as compared to the cost to the company, I am not certain as to whether we were high as to the actual cost of the line.

"Q. That depends on whether the contractor lost money or whether he did not?

"A. That is right. In the case of the St. Joseph 12-inch line the cost to the company was $144,683. Our labor figure on that line comparable to this, is $164,621.

"Q. You were low on that one—are you high or low on that?"

"A. We are high.

"Q. By how much?

"A. By $20,000. Adding the couplings, our figure becomes $190,224, which is the comparable figure with Mr. Black's figure of $157,268.

"Q. Do you know what the experience of the contractor was on that line?

"A. On the St. Joseph line?

"Q. Yes.

"A. No, sir; I do not.

"Q. The next line?

"A. In the case of the new Quapaw 16-inch line, which is the 16-inch line extending from Cotton Valley station, a distance of about 15 miles to the eastward. This line, I believe,

was laid in 1931. The actual cost to the company was $52,899. Our figure comparable with this was $43,147. Adding the couplings our figure is $51,841. Mr. Black's figure is $53,842.

"Q. And in the St. Joseph 16-inch line, which is a 16-inch line extending from a point near Lawrence, Kansas, in a northeasterly direction towards St. Joseph, the actual cost to the company was $62,244?

"A. Yes, sir; our comparable figure is $48,746, adding the joints, our figure becomes $53,582, and Mr. Black's figure is $43,803. In the case of the southern trunk, 16-inch line, this is a 16-inch line extending eastward from Grabham station, a distance of 12 or 15 miles. The actual cost to the company was $95,548, our cost, or the cost used in our valuation $95,622, adding the joints, our figure becomes $111,172. Mr. Black's figure is $86,459. That line was also laid, I believe, in 1931.

"Chairman Greenleaf: You are explaining, are you, the method of adding the couplings? I do not understand that. You say the cost to the company is $95,548?

"A. That is correct. That does not include all items of cost which we have included in our valuation, Mr. Greenleaf.

"Chairman Greenleaf: When you say cost to the company, that don't mean all the cost?

"A. No, sir; that was labor only, and in order to make these figures comparable with Mr. Black's we have had to add in the cost of the couplings, which is material, or in case it happens to be a weld, the cost of the weld.

"Chairman Greenleaf: Now, this first figure of $95,448, at Grabham station, you gave that as the cost to the company?

"A. That is correct.

"Chairman Greenleaf: That includes the pipe and the labor?

"A. No, sir; only the labor, no pipe has been included in those figures, merely labor costs.

"Chairman Greenleaf: And then, the $95,622——

"A. Is the figure which we have used in our valuation, which compares with this actual cost to the company.

"Chairman Greenleaf: Now, then, in the $111,000 plus, [fol. 497] you have added, you say, couplings there?

"A. We have added couplings to make it comparable with Mr. Black's figures, because Mr. Black included his

couplings with the line and if we did not do that, the figure would not be comparable.

"Chairman Greenleaf: It was not clear to me, that was all, I just wanted to get an understanding of it.

"The Witness: In the case of the Topeka 16-inch line, that is a 16-inch line extending from Lawrence, Kansas, to Topeka, the cost to the company for labor was $180,345. The cost as reflected in our valuation for labor was $166,415. If we add to this the cost of the joints, our figure becomes $192,177. Mr. Black's figure is $144,869. The Dillworth-Wellington 20-inch line, the cost to the company was $174,894, our comparable figure to this is $162,915; adding the joints, this figure becomes $176,595. Mr. Black's figure is $163,799. In the case of the Ottawa-Lawrence 20-inch line, that is a 20-inch line extending from Ottawa, Kansas, to Lawrence, Kansas. The cost to the company of the labor was $175,005. Our comparable figure was $151,602. Adding the joints, this figure becomes $177,072, which compares with Mr. Black's figure of $142,030. In the case of the Pampa-Wichita line, this is a line extending from the Pampa Field in Texas, to Wichita, Kansas. The cost to the company was $1,547,013. Our comparable figure to this is $1,832,822. Adding the couplings, or the joints, our figure becomes $2,210,633; Mr. Black's figure is $2,052,519, and in connection with that line I might say it is a well known fact, and has never been disputed, that the contractor lost an amount on that line so that he has never built another major pipe line in this area.

"Q. Is that the extent of your investigations?

"A. That is the list.

"Q. Now, taking this—taking these exhibits, Mr. Eastman, how do the figures you have used in your valuation when worked out, compare with the actual experience of the company on costs? I notice in some you are high and in some you are low. How does it average up over the whole thing?

"A. Based on these lines, I would say that our figures average slightly less than the actual cost to the company; that is, with the exception of this Pampa-Wichita line on which we know the contractor lost a huge some of money.

"Commissioner Hill: What is it, including that?

"A. Including that, I believe they are just about the same.

"Commissioner Hill: Did you total those figures to show what the grand total was?

"A. No, sir; I have not totaled these; that can be done."

There was introduced as exhibit 82, a comparison of costs on construction of the Wichita Ottawa 20 inch line, otherwise known as line "G". Exhibit 82 is a comparison of costs of this line to the company, taken from the company's investment record by C. H. Montgomery, and compared with the allowances by Black in his exhibits 42A, B and C, and with the allowances by Hamilton in his exhibits 17A and B. A comparison with respect to rights of way and damages is as follows:

| | |
|---|---|
| Cost as per company job order 12,145 | $38,427.40 |
| Black's valuation | 54,489.00 |
| Hamilton's valuation | 191,775.00 |

The following exhibit 82 introduced by Montgomery shows in the column headed "As per company J. O. [fol. 4981] 12,145", the actual cost of the construction of the Wichita Ottawa 20-inch line; in column headed, "As per Black and Veatch" is shown the cost of construction of the Wichita Ottawa 20 inch line as found by Black and Veatch, and the column headed "As per F. C. Hamilton Valuation" there is stated Hamilton's estimate of the reconstruction new of said line as follows:

Comparison of Costs on Construction of Wichita-Ottawa 20-inch Line

| | As per company | As per Black & Veatch | As per F. C. Hamilton valuation |
|---|---|---|---|
| 1. Materials | $2,129,143.27 | | |
| Freight | 38,202.17 | | |
| Warehouse expense | 602.20 | | |
| | $2,167,947.64 | $2,029,812 | |
| 2. Labor | 806,310.82 | | |
| Garage, teaming and trucking | 9,797.92 | | |
| | $816,108.74 | 1,008,340 | |
| | $2,984,056.38 | $3,038,152 | $3,572,723 |
| 3. Right of way and damages | 58,427.40 | 54,489 | 191,775 |
| A | $3,042,483.78 | $3,092,591 | $3,764,498 |

| | As per company | As per Black & Veatch | As per F. C. Hamilton valuation |
|---|---|---|---|
| 4. Engineering | $302,768.30 | $154,630 | *$178,636 |
| B | | | $3,943,134 |
| 5. Legal | 2,150.49 | #61,852 | :19,715 |
| Expense Accounts | 11,783.71 | | |
| Incidental expenses | 4,378.92 | | ##39,431 |
| Telephone | 744.15 | | |
| B | $3,304,309.35 | $3,309,073 | $4,002,280 |
| 6. Interest | 24,444.01 | 198,544 | 320,182 |
| Totals | $3,388,753.36 | $3,507,617 | $4,320,460 |
| Deduct items not charged to main line construction | 13,643.26 | | |
| | $3,375,110.10 | $3,507,617 | $4,320,460 |

* 5 per cent of line B column "Hamilton" x $3,572,723.
# Calculated at 2 per cent of A column "Black & Veatch," and includes administration expense x $3,092,591.
: One-half of 1 per cent of line B column "Hamilton" x $3,943,134.
## Applies to $3,943,134 at 1 per cent.

[fol. 499] Eastman compared labor costs to the company with labor costs used by Hamilton in exhibit 17, and by Black in exhibit 41, on eleven major pipe lines, as shown by the following tabulation:

| Line | Company labor | Hamilton | | Black, |
|---|---|---|---|---|
| | | Labor | Labor and couplings | Labor and couplings |
| Hutchinson-Superior | $355,893 | $382,744 | $429,343 | $348,436 |
| Fort Scott 8" | 202,184 | 180,961 | 194,736 | 139,639 |
| Springfield 10" | 380,394 | 442,570 | 489,809 | 343,085 |
| St. Joseph 12" | 144,683 | 164,624 | 190,224 | 157,268 |
| Quapaw 16" (new) | 52,809 | 43,147 | 51,841 | 53,842 |
| St. Joseph 16" (new) | 62,244 | 48,746 | 53,582 | 43,803 |
| Southern Trunk 16" (new) | 95,548 | 95,622 | 111,172 | 86,459 |
| Topeka 16" | 180,345 | 166,415 | 192,177 | 144,869 |
| Dilworth-Wellington | 174,894 | 162,915 | 176,595 | 163,799 |
| Ottawa-Law. Jct. 20" | 175,005 | 151,602 | 177,072 | 142,050 |
| Pampa-Wichita 20" | 1,547,013 | 1,832,822 | 2,210,633 | 2,052,519 |
| Totals | $3,371,012 | $3,672,165 | $4,277,184 | $3,675,769 |

[fol. 500] To make the company's total for the eleven lines comparable with Black's total, Black arrived at the cost of couplings and welds in those lines by deducting Hamilton's allowance for labor of $3,672,165, from his allowance for labor, couplings and welds of $4,277,184, giving $605,019 for couplings and welds; adding this to the company total for labor of $3,371,012, he arrived at $3,976,031 as the company labor total, including couplings, and welds, and arrived at comparable totals as follows:

Company labor cost plus—

| | |
|---|---|
| Hamilton's couplings and welds | $3,976,031 |
| Hamilton—labor cost, including couplings and welds | 4,277,184 |
| Black, labor cost, including couplings and welds | 3,675,769 |

Black prepared the following tabulation, which is a comparison of major labor items involved in pipe line construction, not including painting labor in Black's and Hamilton's valuation:

[fol. 501]

| Size of pipe, inches | 4½ | 6⅝ | 8⅝ | 10¾ | 12¾ | 16 | 18 | 20 |
|---|---|---|---|---|---|---|---|---|
| Weight, pounds per foot | 10.790 | 18.974 | 24.696 | 28.035 | 33.375 | 42.053 | 70.589 | 65.708 |
| Excavation, per foot of line: | | | | | | | | |
| Hamilton | .0540 | .0670 | .0840 | .1030 | .1200 | .1490 | .1670 | .1840 |
| Black | .0470 | .0502 | .0535 | .0693 | .0798 | .1010 | .1062 | .1189 |
| Backfilling, per foot of line: | | | | | | | | |
| Hamilton | .0251 | .0348 | .0410 | .0476 | .0547 | .0662 | .0745 | .0833 |
| Black | .0108 | .0115 | .0122 | .0156 | .0182 | .0231 | .0243 | .0272 |
| Hauling, stringing, laying, per foot of line: | | | | | | | | |
| Hamilton | .0563 | .1026 | .1335 | .1515 | .1804 | .2273 | .2615 | .2552 |
| Black | .1484 | .2372 | .2470 | .2804 | .2920 | .3154 | .5294 | .4025 |
| Jointing, per foot of line: | | | | | | | | |
| Hamilton based on 18-inch lengths | .0883 | .1189 | .1422 | .1767 | .2072 | .2306 | .3706 | .4272 |
| Black | .1100 | .1600 | .2000 | .3300 | .3600 | .4700 | .5300 | .5100 |
| Hamilton's Total | .2257 | .3233 | .4007 | .4788 | .5623 | .7731 | .9936 | 1.0497 |
| Black's Total | .3162 | .4589 | .5127 | .6955 | .7500 | .9095 | 1.1799 | 1.0596 |

[fol. 562] A comparison of the valuation as of Black and Hamilton for this account shows there is a difference of 4½ per cent in the allowances between Black and Hamilton for omissions and contingencies on $26,391,305 worth of pipe, in accounts 1314 and 1333. On the remainder of the difference in these two accounts, or $24,409,515, Hamilton allows a minimum difference for omissions and contingencies of 3 per cent more than Black. Black's allowances for omissions and contingencies on pipe in ½ of 1 per cent on $26,931,305, or $134,657. Hamilton's allowance for omissions and contingencies on this same item was $1,446,565. Black's allowances on the remainder of this account was a maximum of 2 per cent on $24,409,515, or $488,190, and Hamilton's allowance for the remainder of this account was 5 per cent, or $1,220,475. Black's total allowance for omissions and contingencies was $622,847, as against a total allowance by Hamilton of $2,667,040.

Black, engineer for the Commission, prepared the following table comparing overheads on pipe in Accounts 1314 and 1333, showing the overheads used by Hamilton in his valuation and the overheads shown by Mr. Black in his valuation:

[fol. 503]

## Comparison of Overheads on Pipe in Accounts 1314 and 1333

| | Hamilton | | | |
|---|---|---|---|---|
| | Field lines | Main lines | Black, field and main lines | |
| 1. Base Value | 1.000000 | 1.000000 | | 1.000000 |
| 2. Warehousing—5% of field-line pipe only | 0.050000 | | ½ per cent of item 1 | 0.005000 |
| 3. Purchasing, pipe only | | | 1 per cent of item 1 | 0.010000 |
| 4. Supervision and inspection | | | 1½ per cent of item 1 | 0.015000 |
| 5. Subtotal, items 1 to 4, inclusive | 1.050000 | 1.000000 | | 1.030000 |
| 6. Omissions and contingencies—5 per cent of item 5 | .052500 | .050000 | ½ per cent of item 1 | .005000 |
| 7. Subtotal, items 5 and 6 | 1.102500 | 1.050000 | | 1.035000 |
| 8. Engineering—5 per cent of item 7 | .055125 | .052500 | 5 per cent of item 7 | .051750 |
| 9. Subtotal, items 7 and 8 | 1.157625 | 1.102500 | | 1.086750 |
| 10. Organization—½ per cent of item 9 | .005788 | .005513 | ¼ per cent of item 7 | .007763 |
| 11. Law expense—½ per cent of item 9 | .005788 | .005513 | 2 per cent of item 7 | .020700 |
| 12. Taxes—1 per cent of item 9 | .011576 | .011025 | 1.36 per cent of item 7 | .014076 |
| 13. Miscellaneous construction expense—1 per cent of item 9 | .011576 | .011025 | | |
| 14. Subtotal, items 9 to 13, inclusive | 1.192353 | 1.135576 | | 1.129289 |
| 15. Interest—8 per cent of item 14 | .095388 | .090846 | 12 per cent of item 10, 6 per cent of items 14 less 10 | .068223 |
| 16. Subtotal, items 14 and 15 | 1.287741 | 1.226422 | | 1.197512 |
| 17. Cost of financing—4 per cent of item 16 | .051510 | .049057 | | |
| 18. Subtotal, items 16 and 17 | 1.339251 | 1.275479 | | 1.197512 |

[fol. 504] As a check upon the estimates of the respective engineers on rock excavation in Line "G", being a 20-inch line between Wichita and Ottawa, after the decision by the Commission, the plaintiffs accompanied by Geo. P. Reintjes and engineers of the Commission, made actual borings and tests of rock along line "G" in order to determine the actual per cent of pick rock, shoot rock and earth which would be encountered in actual construction. In reference to this new field survey, Mr. Reintjes made an affidavit, stipulated to be considered as his testimony, setting forth his contentions as follows:

"We submit herewith a report of the amount of the rock and earth excavation encountered during the construction of pipe line G between Ottawa and Wichita, Kansas, as estimated on the basis of a recent survey of the entire line. This survey involved actual tests of the nature of the soil along the entire line. The survey was conducted by a party consisting of one of your engineers, Mr. Robert L. Kiddoo; Mr. J. F. Brown, an engineer in the organization of Black and Veatch; the writer; two members of our organization; with assistants for drilling furnished by the pipe line superintendents of the various divisions of the line.

"The rock encountered between Ottawa and Emporia was similar in formation to the Kansas City formation known as the crusher ledge, and a flinty limestone ledge known as the bull ledge, with occasional sandstone outcroppings.

"West of Emporia, the rock in general consisted of an upper formation from 6" to 3'0" thick of very dense flint rock. Underlying it was a dense limestone containing considerable flint or quartz. Below this were several ledges of limestone from 4" to 6" in thickness each. Beneath this was what is known as the Cottonwood Falls limestone which ranged in thickness from 20" to 6'0". The Cottonwood Falls limestone, as well as the ledges immediately above, were comparatively level. The flinty limestone ledge, in places, followed the contour of the hills. The same is true of the flint rock.

[fol. 505] "We dug or drilled two hundred and ninety one holes along the pipe line with a view of using such findings, together with an observation of the amount of rock exposed,

in the pipe line backfill; and exposed ledge outcroppings in determining an estimate of the average amount of rock in each section or square mile traversed by the line. Where the nature of the soil was such that an average estimate could not be placed upon a mile of line smaller lengths ranging down to an eighth of a mile were used. Where rock ledges of some extent were encountered, in order to explore the depth of the ledge, holes were drilled into the rock to a depth below the required trench depth, at intervals of approximately a mile.

"In our estimates we did not consider this strata of shell rock which in our estimation could be broken and removed by the machine ditcher. Nor was the consideration given to extra depth necessitated by highway crossings, etc.

"It is our experience that rock cannot be excavated to a neat depth. It is necessary to excavate by blasting to a depth somewhat below the specified trench depth and backfill to grade with a cushion of earth. Our findings of the quantities of rock summarized by counties as a percent of the specified dimensions of the trench do not consider this extra depth, or overcut. However, in an additional column captioned "Overcut", the amount of such extra excavation expressed as a percent of the specified trench dimensions is tabulated. In the last column are tabulated the percentages of classified excavation allowed by Black.

"We feel that our estimates of the amount of pick and sheet rock in this line are conservative, and that the actual amount of rock taken out by the Contractor in the execution of his contract was probably in excess of these figures.

[fol. 506]

Summary of Rock Excavation, Line G, Wichita–Ottawa 20"

| County | Length | | Shoot rock | | Pick rock | | Total | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Main line | Containing rock | Equivalent Length | % | Equivalent Length | % | Equivalent Length | % | Overcut % | Black's allowance % |
| Butler | 211,144 | 154,313 | 49,353 | 23.37 | 130 | .06 | 49,483 | 23.44 | 10.06 | 10.01 |
| Chase | 83,388 | 73,172 | 42,399 | 50.85 | 270 | .32 | 42,669 | 51.17 | 11.96 | 14.95 |
| Coffey | 36,369 | 2,380 | 216 | .59 | ... | ... | 216 | .59 | .89 | 2.00 |
| Franklin | 87,566 | 39,719 | 17,013 | 19.43 | ... | ... | 17,013 | 19.43 | 6.18 | 12.48 |
| Lyon | 104,635 | 27,928 | 9,772 | 9.34 | ... | ... | 9,772 | 9.64 | 3.64 | [illegible]5 |
| Osage | 97,964 | 36,225 | 15,511 | 15.83 | 66 | .07 | 15,579 | 15.90 | 5.01 | 6.24 |
| Sedgwick | 22,592 | 1,200 | 82 | .36 | ... | ... | 82 | .36 | .79 | 1.24 |
| Totals | 643,658 | 334,937 | 134,346 | 20.87 | 466 | .07 | 134,814 | 20.94 | 7.09 | 10.46 |

[fol. 507]

Survey of Rock Excavation, Wichita-Ottawa 20", Line 6

| County | Length Main line | Shoot rock | | Pick rock | | Total | | Black % |
|---|---|---|---|---|---|---|---|---|
| | | Equivalent length | % | Equivalent length | % | Equivalent length | % | |
| Butler | 211,144 | 49,353 | 23.37 | 130 | .06 | 49,483 | 23.44 | 10.01 |
| Chase | 83,388 | 42,399 | 50.85 | 270 | .32 | 42,669 | 51.17 | 14.95 |
| Coffey | 36,369 | 216 | .59 | ... | ... | 216 | .59 | 2.00 |
| Franklin | 87,566 | 17,013 | 19.43 | ... | ... | 17,013 | 19.43 | 12.48 |
| Lyon | 104,635 | 9,772 | 9.34 | ... | ... | 9,772 | 9.34 | 14.95 |
| Osage | 97,964 | 15,511 | 15.83 | 68 | .07 | 15,579 | 15.90 | 6.24 |
| Sedgwick | 22,592 | 82 | .36 | ... | ... | 82 | .36 | 1.24 |
| Total | 643,658 | 134,346 | 20.87 | 468 | .07 | 134,814 | 20.94 | 10.46 |

[fol. 508] There followed in Reintjes' affidavit details showing the exact location of the 291 holes drilled and the exact conditions encountered, which we deem unnecessary to set out herein.

In reference to this new field survey, Black made an affidavit stipulated to be considered as his testimony setting forth his contentions as follows:

"That I am familiar with Hamilton's exhibits 17a and 17b showing the linear feet of shoot rock and pick rock in the excavation for pipe lines in the transmission systems of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company, and the American Pipe Line Company.

"That when the linear feet of shoot rock and pick rock on each size of pipe line in Hamilton's exhibits 17a and 17b is multiplied by the cubic yards of excavation per linear foot of ditch corresponding to the widths and depths of ditches used by Hamilton in the calculation of costs per linear foot of pipe line in shoot rock at $7.38 per cubic yard, and of pick rock at $4.01 per cubic yard, the results show totals for the system, including line G, of 256,861 cubic yards of shoot rock, and 577,428 cubic yards of pick rock; that the total cubic yards, and total cost of shoot rock and pick rock as calculated from Hamilton's exhibits 17a and 17b, and total cubic yards and total cost of classified excavation covering all classes of rock excavation as calculated from Black's exhibits 41a, 41b, and 41c, is as shown by the following tabulation:

[fol. 509]

| Item | Hamilton | | Black | |
|---|---|---|---|---|
| | Cubic yards | Total cost | Cubic yards | Total cost |
| Shoot rock | 256,861 | $1,895,634 | ..... | ..... |
| Pick rock | 577,428 | 2,315,486 | ..... | ..... |
| Rock, all classification | ..... | ..... | 508,046 | $1,270,115 |
| Totals | 834,289 | $4,211,120 | 508,046 | $1,270,115 |
| Excess—Hamilton over Black | 326,243 | $2,941,005 | ..... | ..... |

"That included in the above tabulation is rock excavation on Line "G", between Wichita and Ottawa, as set out in the following tabulation:

| Item | Hamilton | | Black | |
|---|---|---|---|---|
| | Cubic yards | Total cost | Cubic yards | Total cost |
| Shoot Rock | 35,760 | $263,990 | ..... | ..... |
| Pick rock | 36,722 | 147,584 | ..... | ..... |
| Rock, all classifications | ..... | ..... | 24,000 | $60,000 |
| Totals | 72,482 | $411,574 | 24,000 | $60,000 |
| Excess—Hamilton over Black | 48,482 | $351,574 | ..... | ..... |

[fol. 510] "That Hamilton in calculating the unit costs of pick rock and shoot rock in his exhibits 17a and 17b applied $7.38 per cubic yard for shoot rock and $4.01 per cubic yard for pick rock, to the cubic yards per linear foot of trench determined by the dimensions of trenches set out in exhibit 73, except that in pick rock he used a trench depth 4 inches greater than shown by the exhibit, and that wherever shoot rock or pick rock was found it was calculated as being solid from top to bottom of the trench.

"That I used trench widths and depths shown on pages 18 to 23, inclusive, of my exhibit 42, and that in determining these dimensions I had available 43 pipe-line construction contracts of the Cities Service Gas Company and the Cities Service Gas Pipe Line Company covering a total of 1,673 miles of pipe lines constructed in Texas, Oklahoma, Kansas, Missouri, and Nebraska, towit:

"Contract No. 7736, filed as exhibit 38, covers 242.13 miles of the 20-inch line and 26.46 miles of 12-inch *pipe in* river crossings between Pampa and Wichita, in Sedgwick, Sumner, Harper and Barbar counties, Kansas; Alfalfa, Woods, Woodward, and Ellis counties, Oklahoma; Hamphill, Roberts, and Gray counties, Texas.

"Contract No. 7895, filed as exhibit 81, covers 25.11 miles of 20-inch pipe line, 4 miles of 16-inch, 0.8 miles of 4-inch, 1.73 miles of 6-inch, and 4.48 miles of 8-inch pipe lines, in Gray, and Carson counties, Texas.

"Contract No. 8072, filed as exhibit 80, covers 139.62 miles of the Wichita-Ottawa 20-inch pipe line, made up of 121.9 miles of 20-inch and 14.52 miles of 16-inch and 3.20 miles of 12-inch pipe line in river crossings, in Butler, Chase, Coffey, Franklin, Lyon, Osage, and Sedgwick counties, Kansas.

"Contract No. 8302, filed in this case as exhibit 78, covers 43.5 miles of 8-inch gas pipe-line in Allen and Bourbon counties, Kansas, between the Petrolia station and Fort Scott.

"Contract No. 8314, filed in this case as exhibit 79, covers 70.6 miles of 10-inch, 8.7 miles of 3-inch, 0.39 miles of 2-inch, and 3.3 miles of 6-inch main and branch lines in Newton, Lawrence, Christian and Greene counties, Missouri.

"Contract No. 6553, covering 33.71 miles of the Davenport-Lindley line in Creek and Lincoln counties, Oklahoma,

and consisting of 4.05 miles of 8-inch, 8.70 miles of 10-inch and 20-96 miles of 16-inch pipe line.

"Contract No. 7419, covering 5.83 miles of 6-inch pipe line in Okfuskee county, Oklahoma.

[fol. 511] "Contract No. 7434, covering 12.66 miles of 6-inch and 12.02 miles of 8-inch pipe in the Bearden-Papoose-Seminole gas-gathering system in Okfuskee, Hughes and Seminole counties, Oklahoma.

"Contract No. 7511, covering 30.14 miles of 16-inch gas line in Creek, Okfuskee, and Seminole counties, Oklahoma.

"Contract No. 7524, covering 6 miles of 12-inch line in Seminole, Okfuskee and Hughes counties, Oklahoma.

"Contract No. 7563, covering 10.18 miles of 8-inch gas pipe line in Kay and Grant counties, Oklahoma.

"Contract No. 7612, covering 5 miles of 12-inch line in Seminole county, Oklahoma.

"Contract No. 7799, covering 14.63 miles of 12-inch gas pipe line in Osage county, Oklahoma.

"Contract No. 7846, covering 11.96 miles of 16-inch line in Allen county, Kansas.

"Contract No. 7927, covering 2.62 miles of 6-inch line in Hughes county, Oklahoma.

"Contract No. 8028, covering 5.33 miles of 8-inch gas line in Gray county, Texas.

"Contract No. 8059, covering 2.06 miles of 8-inch and 6-inch line in Carson county, Texas.

"Contract No. 8090, covering 5.97 miles of 12-inch line in Leavenworth county, Kansas.

"Contract No. 8091, covering 38.75 miles of 16-inch line in Franklin, Douglas and Johnson counties, Kansas.

"Contract No. 8095, covering 6.67 miles of 8-inch line in Osage county, Oklahoma.

"Contract No. 8123, covering 7.30 miles of 8-inch gas pipe line in Lyon county, Kansas.

"Contract No. 8129, covering 26.93 miles of 12-inch gas line in Leavenworth county, Kansas, and Platte and Buchanan counties, Missouri.

"Contract No. 8149, covering 11.64 miles of 4-inch pipe line between the Wichita-Ottawa 20-inch main line and the Madison, Kansas, gasoline plant, in Lyon and Greenwood counties, Kansas.

"Contract No. 8210, covering 15 miles of 4-inch and 10-inch line in Newton county, Missouri.

"Contract No. 8247, covering 8.31 miles of 16-inch and 1.23 miles of 2-inch line in Washington and Nowata counties, Oklahoma.

"Contract No. 8282, covering 19.47 miles of 20-inch line and 15.07 miles of 16-inch in line Douglas and Franklin counties, Kansas.

"Contract No. 8283, covering 9.23 miles of 6-inch line in Seminole county, Oklahoma.

"Contract No. 8289, covering 28.42 miles of 8-inch line in Rice and Reno counties, Kansas.

[fol. 512] "Contract No. 8292, covering 28.42 miles of 8-inch line in Kay, Noble and Logan counties, Oklahoma.

"Contract No. 8321, covering 15.81 miles of 12-inch, 4.04 miles of 10-inch and 1.29 miles of 6-inch line in Logan county, Oklahoma.

"Contract No. 8328 and 8328-A, covering 39.5 miles of 8-inch, 11.4 miles of 6-inch, 16.62 miles of 4-inch and 8.86 miles of 2-inch line of the Atchinson Falls City, Neb., line, in Atchinson and Brown counties, Kansas, and Richardson, Nebraska.

"Contract No. 8341, covering 10.86 miles of 6-inch line in Okfuskee county, Oklahoma.

"Contract No. 8376, covering 39.19 miles of 20-inch and 10 miles of 24-inch line from Logan county to Oklahoma City, Oklahoma.

"Contract No. 8399, covering 5.90 miles of 16-inch line in Douglas and Shawnee Counties, Kansas.

"Contract No. 8400, covering 40.29 miles of 2-inch, 14.55 miles of 3-inch, 58.94 miles of 4-inch and 116.28 miles of 8-inch line in Rice, Ellsworth, Lincoln, Mitchell, Osborn, Jewell and Smith counties, Kansas, and Nuckolls county, Neb.

"Contract No. 9421, covering 14.96 miles of 16-inch line in Montgomery and Labette counties, Kansas.

"Contract No. 8460, covering 5 miles of 6-inch line in Carson and Gray counties, Texas.

"Contract No. 8466, covering 31.37 miles of 20-inch line between Dilworth, Okla., and Wellington, Kans., in Kay county, Oklahoma, and Sumner county, Kansas.

"Contract No. 8467, covering 109.23 miles of 12-inch line between Ottawa, Kansas, and Sadalia, Mo., in Franklin and Miami counties, Kansas, and Cass, Johnson and Pettis counties, Missouri.

"Contract No. 8476, covering 9.09 miles of 16-inch line in Douglas and Leavenworth counties, Kansas.

"Contract No. 8481, covering 25.73 miles of 3-inch line in Lincoln and Ottawa counties, Kansas.

"Contract No. 8501, covering 44.17 miles of 8-inch, 21.90 miles of 6-inch, 16.90 miles of 4-inch and 7.65 miles of 3-inch line in Johnson, Carroll, Lafayette, and Saline counties, Missouri.

"That I made my classification of excavation by inspection of the location of the lines and by my knowledge of the territory through which these lines ran; that in addition to allowing earth excavation on all lines to the full depth of trench at 35 cents per cubic yard, I also allowed in the same ditch classified excavation to cover all classes of rock, including shoot rock or pick rock, at $2.50 per cubic yard for whatever per cent of the excavation I found as rock, or, in other words, I allowed $2.85 per cubic yard for rock excavation.

"That T. R. Jones, who constructed line G between Wichita and Ottawa, under a contract filed as exhibit 80, testified that "a little over 75 cents' per linear foot was [fol. 513] a fair price for rock excavation on this line in a trench 28 by 40 inches (tr. 2247); that this is equivalent to a price of $2.60 per cubic yard for solid rock. (Agreed statement of facts and agreed abstract of the evidenec. P. 35.)

"That from October 7 to 16, inclusive, 1932, a field party under the direction of George P. Reintjes and Robert L. Kiddoo for the respondent, with J. P. Brown as an observer for my office, made measurements at 291 points along line G between Wichita and Ottawa for the purpose of determining the actual quantities of rock involved in its construction; that the points at which these measurements were made were selected primarily because rock showed in the trench backfill, and that all other sections of the line were excluded from the survey on the theory that only earth excavation would be encountered; that 234 soundings were made to determine the depth of cover over the pipe, and 291 soundings were made to determine the depth to rock in undisturbed earth, and that the thickness of rock was generally determined by deducting the depth to rock in undisturbed earth from the depth of pipe cover plus the 20-inch outside diameter of the pipe; that 38 borings

were made through the rock to the plane of the pipe bottom.

"That although this survey established the fact that the depth of trench in line G averaged 48.72 inches instead of 44 inches, the depth used by both Hamilton and Black in the calculation of rock quantities in Hamilton's exhibits 17a and 17b and in Black's exhibit 41a and 41b, that Reintjes calculated the per cent of rock exclusive of alleged overbreak on the basis of a 44-inch depth of ditch instead of on the actual and greater depth of ditch determined by the resurvey; that, for illustration, Reintjes shows that at survey hole No. 149, Butler county, Kansas, the depth of earth over rock was 34 inches, and that the thickness of rock above pipe bottom was 18 inches, the depth of ditch to pipe bottom was 52 inches; that Reintjes calculates the percentage of rock at this point by dividing the 18 inches by 44 inches which results in 40.9 per cent of rock instead of 34.6 per cent, the correct figure as shown by this test hole if the 18 inches, the depth of rock, is di-
[fol. 514] vided by 52 inches, the actual depth of trench.

"That Reintjes estimates it is necesary to excavate the trench in rock 6 inches below pipe bottom to allow for alleged overbreak, and that he calculated this per cent of overbreak on the basis of a 44-inch depth of ditch, instead of on the actual and greater depth determined by the survey, and that using survey hole No. 149, Butler county, Kansas, this percentage as calculated by Reintjes is 6 inches divided by 44 inches, or 13.6 per cent, instead of 10.3 per cent, which figure results from the division of 6 inches by 58 inches, the actual depth of trench including alleged overbreak; that the 7.09 per cent of alleged overbreak in the tenth column of Reintjes' survey summary is obtained by applying the percentage found by dividing 6 inches of overbreak on 334,937 feet of line G covered by the survey by a trench depth of 44 inches and applying it to the total length of 643,658 feet in line "G".

"That the resurvey of line G disclosed no basis for the calculation of overbreak, if any, below the bottom of the pipe as laid. That the contractor on Line G was required to cover this line a specified minimum cover in "shoot rock" and a specified minimum cover in earth and "pick rock," and that he was required to perform all the ditching and backfilling in all classes of excavation, as well as certain other construction operations, for a specified price per foot of line regardless of the character of quantities

of materials excavated in order to secure the minimum cover specified. (Exhibits 80 and 77.) That the resurvey of line G shows the following quantities of classified excavation and the quantity of rock excavation included in Hamilton's exhibits 17a and 17b and in Black's exhibits 41a, 41b and 41c.

[fol. 515]

| Item (Vol. 1) | Hamilton Exhibits 17a and 17b (Vol. 2) | Black Exhibits 41a, 41b and 41c (Vol. 3) | Resurvey Reintjes excluding overbreak (Vol. 4) | Resurvey Reintjes including overbreak (Vol. 5) | Resurvey Brown (Vol. 6) |
|---|---|---|---|---|---|
| Trench width and depth in earth and "pick rock" | 39" x 44" | 30" x 44" | 39" x 44" | | 39" x 50" |
| Trench width and depth in "shoot rock" | 39" x 40" | 30" x 44" | 39" x 44" | | 39" x 48.7" |
| Cubic yards of "shoot rock" | 35,771 | | 48,655 | 65,901 | 46,619 |
| Cubic yards of "pick rock" | 30,804 | | 163 | | 170 |
| Cubic yards of rock of all classifications | 79,575 | 94,000 | 48,818 | 65,901 | 46,789 |

[fol. 516] "That if the allowance for rock on line G is made on the basis of Brown's calculations from the resurvey there should be added to Black's total allowance for account 1333 —

| | |
|---|---|
| 46,789 cu. yds. of rock @ $2.50, or | $116,972.50 |
| Less 24,000 cu. yds. of rock @ $2.50 | 60,000.00 |
| Or a net addition of | 56,972.50 |

"That if alleged overbreak should be added on the basis of Reintjes' calculations there should also be added 16,546 cu. yds. of rock excavation at $2.50 or a total of $41,365.

"That I have made a calculation of the average outside diameter of pipe in the transmission systems involved herein and that the average pipe in rock excavation is under 12 inches outside diameter, and if laid in the same location as line G there would be an average, but not an actual, decrease of 8 inches in the depth of rock excavation and an actual decrease of 8 inches in the width of trench, and that the per cents of rock excavation developed by the resurvey of line G cannot fairly be applied to that part of the total system on which rock is encountered.

"That the following tabulation is a summary by counties, showing total trench excavation, total rock excavation, the ratio in per cent of solid rock and "pick rock" to total excavation, as calculated from the date obtained by Brown in the resurvey of Line G. The calculation of the above data by land section is attached hereto.

[fol. 517]

Summary of Counties of Rock Quarries in Line G Calculated from Records of October 7 to 16, 1882.

| County (1) | Length along center line: Gross feet (2) | River crossings, feet (3) | Net feet (4) | Total solid cu. yds. (5) | River crossings, cu. yds. (6) | Net cu. yds. (7) | Total rock excavation: Solid cu. yds. (8) | Pink cu. yds. (9) | Ratio of rock excavation to total solid excavation: Solid Per cent (10) | Pink Per cent (11) |
|---|---|---|---|---|---|---|---|---|---|---|
| Franklin | 91,449 | 4,532 | 86,917 | 38,286 | 1,728 | 36,558 | 4,982 | 0 | 12.97 | 0.00 |
| Osage | 96,633 | 271 | 96,362 | 40,152 | 226 | 39,926 | 5,577 | 0 | 13.97 | 0.00 |
| Coffey | 96,369 | 0 | 96,369 | 14,959 | 0 | 14,959 | 0 | 0 | 0.00 | 0.00 |
| Lyon | 130,195 | 25,560 | 104,635 | 33,153 | 20,520 | 12,633 | 5,088 | 0 | 7.28 | 0.00 |
| Chase | 93,998 | 0 | 93,998 | 33,468 | 0 | 33,468 | 55,089 | 0 | 62.65 | 0.00 |
| Butler | 223,540 | 12,396 | 211,144 | 26,473 | 5,202 | 21,271 | 25,204 | 0 | 62.56 | 0.00 |
| Sedgwick | 22,392 | 0 | 22,392 | 9,286 | 0 | 9,286 | 29 | 0 | 0.22 | 0.00 |
| Totals | 696,168 | 42,399 | 643,209 | 277,777 | 17,882 | 259,895 | 46,424 | 398 | 17.95 | 0.17 |

[fol. 518] Interest During Construction

The evidence on Interest During Construction was submitted to the District Court on the following agreed-statement:

"Hamilton allowed for this item $6,337,986.00, which he did not depreciate. Black allowed $4,345,125.00 new and $3,868,428.00 depreciated. The Commission allowed for the item $3,883,282.00 the difference between that allowance and the amount claimed by Hamilton being $2,454,704.00.

"The allowance made by the Commission is the allowance made by Black adjusted in accordance with changes made in his valuation of the property.

"As to the basis for his allowance Black testified as follows:

* * * 'Q. The next item is interest during construction $4,345,125.00. How did you arrive at that?

'A. Interest during construction has been arrived at on the basis of a two-year construction period, using an interest rate of six per cent. I have assumed, however, that all land and rights of way would necessarily be acquired early in the construction period; for that reason I have allowed two years' interest, or twelve per cent on all lands and all rights of way.

'Q. Is that depreciated?

'A. Interest during construction is applied also to all property accounts plus engineering and superintendence, administrative and legal expenses and taxes during construction.

'Q. In other words to all items appearing on this summary above the item of interest during construction?

'A. Excepting preliminary organization expenses, that is not applied there.

'Mr. Stone: On the rest of the construction an average of two years in the one year?

'A. Yes, sir. * * *

'Q. Is that depreciated?

'A. Yes, sir.'

"Black further testified that he allowed interest at the rate of 6% for one year on all physical property except land and rights-of-way on which he allowed 6% for two years or a total of 12%; that he took two years as the con-

struction period; that he assumed part of the system would be placed in operation before the completion of the entire project and for that reason eliminated half the construction period; that he did this on the theory that 'you have your investment only for half the period; * * * that you are only going to have your investment in certain items that enter into the property of this kind during half of the construction period and for that reason 6% is the interest return on the entire construction period, just based on the average time'; that in his opinion the rate of interest [fol. 519] during construction should be different from the rate of return on the project after it is placed in operation. The witness was not asked and did not state any reason for this difference in rate of return other than his own opinion.

"Hamilton testified that he used 8% based on a two-year construction period and therefore allowed 8% for one year; that his 8% was figured on the same amount as that on which organization and legal expenditures are figured plus total of organization, legal expenditures, taxes during construction and miscellaneous construction expenditures; that he did not assume the plant would be in operation during the construction period of two years and that no income would result from operation during that period."

Going Value

It was agreed by the parties before the District Court that the following agreed statement on going value should be submitted as the evidence on that account:

"Black allowed in his valuation for this item $3,820,000.00 and Hamilton $8,898,532.00, the difference between the two engineers being $5,078,532.00. The Commission found a going value of $2,000,000.00 on the reasoning set out in the opinion at pages 85 to 88.

"In regard to going value, Black testified (T. pages 1873-1874) as follows:

'* * * Q. The last is going concern value, $3,820,000.00. How did you arrive at that amount?

'A I have considered going concern value at it is normally considered, I think, as being the difference between a plant all ready to operate and not operating, and a plant all ready to operate with customers attached. I have taken as

the best measure of certain items of that going value the company's operating experience, and briefly I have allowed in arriving at this figure used here, $15,000.00 for the books and records of the company, I have allowed $1,020,000.00 for organization of the operating company, that is the organization of the company, and I have allowed interest and depreciation on idle plant, plant that would be idle during the period this company is acquiring its business, that is between the end of the construction period and the time all business is attached, in the amount of $2,784,645.00, added to the two other amounts of $15,000.00 and $1,020,000, gives $3,819,645.00, which I have applied as $3,820,000.00.

[fol. 520] 'Q. Is that depreciated?

'A. No sir, it is apportioned among the properties of the various states directly in proportion to the cost of reproduction of property in those states bears to the cost of the reproduction of the total property. * * *"

"And again on pages 2178 and 2181 as follows:

"* * * I have computed my allowance for going concern value on the basis that it is best measured by the cost of reproducing the business of the company and I have allowed in my calculations for going concern value for books and records of the company, for organization, for interest on idle plant and for depreciation on idle plant.

'Q. Those are the items that have entered into the total you have given in your calculation?

'A. Yes, sir, $3,820,000, rounded out.

'Q. Have you those figures broken down into the different items entering into the totals?

'A. Yes, sir.

'Q. Let us have those, please?

'A. I have books and records of the company at $15,000.00. These books of course are the records or whatever they may be, are in addition to the property records, etc., which you have accumulated during the time of your construction. I have allowed $1,020,000 for organization, I have allowed a total for interest on idle plant and depreciation on idle plant of $2,784,645.

'Q. That is 6% interest?

'A. No, that is on the basis of 8%.

'Q. And what rate of depreciation, please?

'A. Two and one-half per cent.

'Q. What was that amount?

'A. Two and one-half.

'Q. I mean, the amount of this two items in dollars?

'A. $2,784,645.

'Q. What are the other items, please? Is that all of that, does that make the total amount allowed?

'A. This is—yes, it totals to $3,819,645, and we have used $3,820,000.

'Q. The 8 per cent you have allowed for interest and 2½ per cent for depreciation, would make a total of 10½ per cent that you have applied to the idle plant, is that the idea?

'A. That is true, sir.

'Q. Well, if those two figures total 10½ per cent which are applied to the idle plant it would have to be $26,500,000 to give that figure by applying 10½ per cent, would it not?

'A. I did not apply it that way.

'Q. I would like to have that?

'A. Well on the basis of having 50 per cent of the business attached at the end of the construction period and 100 per cent at the end of the second year, I have in my calculation for interest on idle plant, I have 30 per cent of my plant idle for one year and 5 per cent idle for one year, at 8 per cent, that works out to .028, as applied to the entire property, and results in the figure. I have not separated that figure after applying it to the total property, but I have added all my depreciation on idle plant in the same calculation, that is in percentage.

[fol. 521] 'Chairman Greenleaf: Just as a matter of information, what is the idle plant? Just what do you refer to there, just roughly?

'A. I am assuming that, in the construction of this property as it exists today, that we are attaching business, certain capacity of this plant that is not required.

'Chairman Greenleaf: I understand now. I did not know to what you referred.

'A. Yes.

'Q. Are you assuming that on the completion of the plant, the entire project, at the end of a two-year period that all of its business will be attached at that time?

'A. No, sir, 50 per cent of it.

'Q. Fifty per cent?

'A. Yes, sir.

'Q. Then at the——

'A. You are talking about the construction period now?

'Q. Yes, you assume two years' construction period?

'A. Yes, sir.

'Q. At the end of two years, the project will be completed?

'A. That is correct.

'Q. What percentage of business do you assume will be attached at that time?

'A. Fifty per cent at that time.

'Q. And at that time 50 per cent of the plant would be idle?

'A. Yes, if there is 50 per cent of it not built—you mean at the end of the construction period?

'Q. Yes, 50 per cent of the plant would still be idle and earning nothing on the investment?

'A. Yes, that is right. * * *'

"Hamilton testified, on cross-examination as follows:

'* * * Q. Now, we come to going concern value. That is $8,898,532.00?

'A. Yes, sir.

'Q. Is that a percentage of anything?

'A. That is 10 per cent.

'Q. Of what figure?

'A. That is 10 per cent on all of the items up to and including the cost of financing, but excluding working capital and materials and supplies.

'Q. Working capital and materials and supplies is the only thing excluded?

'A. That is the only thing excluded, yes, sir.

'Q. How did you arrive at that amount?

'A. I have just taken 10 per cent of the physical property value for this particular case, for that item.

'Q. You have not itemized it?

'A. No, sir, I have not itemized it in any way.

'Q. You have not taken into consideration the fact that in the reproducing new this system, that you are wholesaling gas and that you have your markets already provided?

'A. You could not possibly have your markets already [fol. 522] provided, because it takes a distributing company at least three years to get their customers up to a

reasonable consumption of gas, after they have started putting in the appliances. You have a place to sell gas, but you cannot sell it until they in turn get their customers to buying it.

'Q. You would not include in this any expenses the distributing companies have?

'A. No, we would include in this no cost the distributing company has to take, because of their expenses in getting customers, but we do include in this cost the carrying pipe line capacity that is idle a portion of the time until you get up to the load for which it was ultimately, or for which it was designed.

'Q. But in this case, here, these distributing companies are already functioning and furnishing gas?

'A. They would not.

'Q. And all that the pipe line company would have to do would be to get the gas to the city gates and turn on the gas, isn't that all they would have to do?

'A. No, for the simple reason that the gas companies would not be functioning and furnishing gas until such time as the pipe line company had——

'Q. You mean their relationship is such that they could not exist without the pipe line companies?

'A. Not as natural gas companies, that is perfectly true.

'Q. Some of these concerns were furnishing gas at the time you purchased them, were they not?

'A. Furnishing——

'Q. Some of these distributing companies?

'A. Of course, because the pipe line had been constructed for years.

'Q. Your company wholesales gas, as I understand?

'A. That is true.

'Q. You don't furnish any gas to domestic consumers?

'A. There is some slight exception to that where we run through farms, or something like that but they don't mean anything.

'Q. How many customers do you have to which you wholesale gas, in round numbers, I don't care to have it exact.

'Mr. Stone: You mean including distributing companies.

'Mr. Welch: Yes, sir.

'A. I cannot tell, because I don't know how many main line industrial consumers there are. We have some.

'Q. Omitting the main line industrial consumers, how many customers do you have to which you furnish gas.

'A. Oh, I presume at least a hundred.

'Q. For instance, take the City of Wichita, this system does pipe the gas there and turn it over to the distributing company?

'A. To the town border, and in my estimate of a hundred I have included Wichita as one.

'Q. Now what do you include in the elements of going value, Mr. Hamilton?

'A. What I have included in the value of the business attached and operating, and yielding a revenue, and I have done it on the basis of experience with the cost of getting a system into that sort of shape.

[fol. 523] 'Q. As I understand, then, you did not arrive at it by finding the cost of attaching this business.

A. It is partially the cost of attaching the business, and the time of the engineers and others in negotiating the contracts, but that, for a wholesale situation, is a small item. The largest cost is the excess capacity that you will have to have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on.

Q. Do you think that if you should reproduce your plant new and then go to the Wichita distributing company that you would have any trouble negotiating a contract with them to turn them over the gas?

A. No.

Q. Would that be true with reference to the Western Distributing Company?

A. It would be perfectly true, but we would not have any trouble about it, but we would have to determine what amount they had and reach an agreement on that.

Q. Well your plant is constructed here, with the idea of selling all the gas you can get a market for, isn't it?

A. Yes.

Q. So whatever amount they might want you would be very glad to turn it over to them at what you determined to be the price at the gates?

A. That is true, but we would have to arrive at some conclusion as to what that amount would be.

Q. That wouldn't take very long, would it?

A. Yes, it would take some considerable time, and a lot of judgment, if you were going into a town that didn't now have natural gas, you would have to make a pretty careful——

Q. You assume those towns don't have natural gas. We are today talking about the proposition of reproducing this pipe line now.

A. Yes, sir.

Q. You know just exactly where you want to go, you know you want to go to Wichita, you know you want to go to Ottawa, you know you want to go to Topeka, you know you want to go to Kansas City, Missouri, and places of that kind, and so far as that is concerned, there is nothing unknown about that, you know exactly what you want to do, you know that you want to furnish gas at these various towns, because you are building your pipe line up to them, and you know in most of the towns that there is a distributing company there, with a market that wants to buy gas of you, isn't that true?

A. That is very true.

Q. Now in constructing this pipe line, reconstructing this pipe line, if you had to reconstruct it now, what would be the best place to commence after you had your gas fields established, and in view of the fact that you have your gas purchase contracts?

A. It would be at the field. What you would do, as a practical matter, is commence at half a dozen different places as we do. In other words, very seldom will you find a contractor with a force, or equipment ready to take a contract for a whole pipe line. It is let by sections, so you actually commence construction in several different places.

Q. Now having in mind this particular pipe line, where in your opinion would it be best to commence constructing this line and to what points?

A. Well, I think you would commence constructing this at the various fields, and moving toward the towns as rapidly as you could.

[fol. 524] Q. One of the largest fields that you buy gas from is the Oklahoma City Field?

A. Yes, sir.

Q. And that line would be constructed from there among the first, wouldn't it?

A. Yes.

Q. And that line in a short time could be supplying the city of Wichita, I take it?

A. Well, I don't know what you mean by a short time, but you could not get that line constructed in less than a year, I don't believe.

Q. Well, probably when I said short time, that is pretty indefinite, but after you had that line constructed, inside of a year, you could be furnishing gas to the city of Wichita?

A. That would be possible, yes, sir.

Q. Now, while you are building that line, what other lines would you think should be built?

A. I think the Amarillo line would be started, also.

Q. That would also go toward Wichita?

A. Yes, sir.

Q. And what line would you build next?

A. I think we would build north toward Kansas City from the Oklahoma City line, and also across from Wichita toward Ottawa, and into Kansas City.

Q. While you were building those lines from Oklahoma City to Wichita, there is no reason why you could not be engaged in constructing these other lines you have spoken about?

A. That is perfectly true.

Q. They could be all built at the same time?

A. With certain limitation, that is that in such a large project as this, there are only certain contractors with the credit and experience to take the contracts and be able to carry them out.

Q. In other words, on such a vast system there would be some difficulty in getting competent contractors to handle it?

A. Not only contractors, but labor. If you tried to hurry it you would have a lot of contractors bidding for labor and your labor costs would be up.

Q. But in the meantime, while you were constructing this pipe line, it would be good business to commence to furnish the cities along this line just as soon as you could?

A. Just as soon as you could.

Q. Do you know, Mr. Hamilton, how long it took to construct the line from Amarillo to Chicago?

A. From Amarillo to Chicago, it took about fourteen months, as I remember, from the time they started.

Q. That was a 24-inch line, as I remember it?

A. Yes, sir.

Q. The line from Amarillo to Wichita, that, as I understand, when it was built, was built for the purpose of taking care of the demand you had for gas at that time?

A. Yes, sir.

Q. You already had the demand for gas, and the Amarillo line was put in for the purpose of taking care of the demand at that time, that had already accumulated?

A. To take care of it, based on the disappearing supply with which we had previously been taking care of it.

Q. I understand that, but the Oklahoma line was built [fol. 525] to take care of a demand that you then had for gas?

A. Yes, it was with the idea of supplying ourselves with gas at a cheaper price than we had been forced to pay, otherwise, before this field came in.

Q. You already had the demand for the gas?

A. Yes, and we already had a source of supply, but this was a cheaper source.

Q. Where is your large demand for domestic use, Mr. Hamilton, the two Kansas Cities?

A. The two Kansas Cities.

Q. Of course, you have had these two Kansas Cities for a long time?

A. Yes, sir.

Q. And the demand there on account of the industrial gas, you have been furnishing, has been becoming larger in the last three or four years?

A. No, because the only thing we consider in the demand is our peak demand—that is the thing that bothers us. What has been happening is the domestic consumers when we bought the plant were using gas on a basis of some 40,000 feet and now they are using 67,000, as I remember it.

Q. When you bought it what was the industrial demand?

A. There was none.

Q. What is it now?

A. It is very large now.

Q. It is considerably more in thousand cubic feet than the domestic, is it not?

A. Not than the maximum domestic, no. In the summer time it is very much more.

Q. The total amount of gas furnished per year in Kansas City, for industrial, how does it compare with the total amount furnished in Kansas City for domestic?

A. I cannot tell you that offhand.

Q. Is it more, or less?

A. I cannot tell you that, even. I can find out, very easily.

Q. Do you have it in the exhibits that have been furnished?

A. I think it is one of these exhibits, but I don't know whether it is segregated as to Kansas City or not.

Mr. Stone: It is in the earnings statement.

The Witness: Kansas City Gas Company, the domestic sales here for the year ending June 30, 1931, were 7,985,826 M. cubic feet, and the industrial sales were 7,070,343 M. cubic feet. In other words, the industrial sales are about eleven or twelve per cent less than the domestic sales.

Q. What was it for the year ending December 31st?

A. For December 31st, 1930, the domestic was 7,410,603 M. cubic feet, just about ten per cent more in industrial than domestic.

Q. When was it you first took on the furnishing of industrial gas in the Kansas Cities, Mr. Hamilton?

A. I don't believe I can tell you that. It was some time ago, however.

Q. You cannot tell us the date?

A. No, I cannot, because I am not familiar with the operations except in a general way.

Q. How many lines do you have into Kansas City?

A. Three.

[fol. 326] Q. One of those was built rather recently, Mr. Hamilton?

A. I don't know the date of it. I know it was rather recently but I cannot tell you the date.

Q. That was an additional line to take care of increased capacity there, at Kansas City?

A. Yes, it was. * * *

"Hamilton further testified, on cross-examination (T. 1572-1574), as follows:

"* * * Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant, or something like that, there might be a wholly different basis.

Q. For instance you take the distribution plant, take the one herein Topeka, for example——

A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

A. That is true, and ten per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

A. That is true.

Q. That should be taken into consideration in arriving at the going value in this case?

A. That is true.

Q. Then I take it you should take into consideration the fact here that the towns supplied by this pipe line company, with the exception of perhaps Superior, Nebraska, and those on that line west are accustomed to using natural gas. Kansas City, Topeka, Wichita, Ottawa, and towns of that kind have used natural gas for years, isn't that true?

A. That is what makes this pipe line valuable, because they have used it, and are in the habit of using it, and don't want to use anything else.

Q. And you should take into consideration that the building of this pipe line to those towns, those towns that already have been educated to be using natural gas?

A. You should not take it into consideration when you are arriving at a going concern value, no, sir, because that is what makes the going concern value.

Q. Well, if it does make it it should be taken into consideration?

A. Yes, sir.

Q. I thought you said it should not be.

A. It should not be to reduce it, because it makes the going value.

Q. You mean to say it should not be taken into consideration to make it less?

A. I make a distinction between that and a town which has not been using gas, after you get it up to normal consumption.

Q. Then I understand in arriving at this going value, when you furnish gas to a distributing company that is in a town that has never used gas before, you say in cases of that kind there is a period of time before the people will be educated to using gas, and therefore if they are now educated to using gas, your going value should be that much more, is that the idea?

[fol. 527] A. No, it should be the same in both towns after they get up to the normal use of gas. Now at the time the pipe line is first constructed to new towns that have not used gas, its going value would be less during those years, while they were getting up and getting into that condition of carrying the full load.

Q. The cost of attaching the business, if you supply that gas to a company in a town where they are already educated to taking gas, it would not take so long there, and the expenses of acquiring the business would not be near as much?

A. If you could presuppose some other pipe line had been supplying this town with gas, and today they could cut off and tomorrow we go in, it wouldn't take any time, but that isn't the conditions under which pipe lines are built. * * *"

"Jarboe, superintendent of all pipe lines of the system, testified that the line to the Amarillo field was constructed for the purpose of taking care of the present demand of the pipe line system.

"Hamilton testified on cross-examination:

'Q. The line from Amarillo to Wichita, that as I understand, when it was built was built for the purpose of taking care of the demand for gas you had at that time?

'A. Yes, sir.'

"Hamilton on redirect examination testified as follows (T. 1563-1574):

"* * * Q. Would you say there was an element of value to a pipe line system such as the Cities Service Gas Company in having the distributing companies in its major

markets associated with it so that its markets were sure to continue to the pipe line company?

A. There is a value in that, of course. There is not only a value in that factor, but there is also a value in the harmonious working with the distributing company in the handling of your load.

Q. Is it not true that these distributing companies were purchased by Cities Service Gas Company for the reason that it considered it necessary to have a harmonious working agreement between pipe line company and the distributing company?

A. That was one of the reasons, the other was to get better practice in the distributing companies from an engineering and operating standpoint.

Q. Those distributing companies when purchased were all losing money, were they not?

A. Practically all of them. None of them were making a fair return.

Q. Isn't that an element that enters into the going value you have used, the fact that these companies are associated, their practices have been controlled, and their business built up in the manner it has been?

A. That is perfectly true.

Q. When a pipe line is built to a town that has not had gas before, is it true that the business comes to the distributing company immediately, or does it take a period of time to attach that business?

A. It takes a period of time and a lot of expenditure of effort to get it.

Q. The pipe line from Hutchinson to Superior, Nebraska, which has been built about a year, that pipe line is not at this time making a return at all, is it?

A. Oh, no.

[fol. 528] Q. And it won't be for a number of years, takes time to build up that business?

A. That is perfectly true, and even when you build it, as we did, renewed a line to St. Joe, where they had previously had natural gas and then had used artificial gas for a few years there, the consumption is not near, and won't be for some time, up to what we finally expect to get it, and not up to the figures for which the pipe line was designed originally.

Q. The acquisition of the Kansas City Company was referred to. I will ask you if prior to the acquisition of that company by the Cities Service group, the relations between the pipe line company and the distributing company were friendly or unfriendly?

A. They were unfriendly.

Q. There had been considerable litigation between the two companies, had there not?

A. Almost endless.

Q. I will ask you whether you have any information in regard to the Chicago pipe line, as to whether any cities were attached to that line or any gas put through it prior to the time the line as a whole was constructed?

A. No gas except for testing purposes.

Q. So that line was not completed part way and then put in operation as to a part of the total market, but was entirely completed before it was utilized in any respect?

A. That is true.

Q. Are you certain as to the fourteen months you testified to that it took to construct that line? Wasn't a considerably greater period, all of two summers and one winter?

A. I am talking about the actual time of construction.

Q. Well, if you don't know, I don't want you to guess at it, but I think you are in error about it. In that job, and in any other similar job it would be necessary to order the pipe a long time——

A. I am not talking about time for design of the pipe line, or time spent working our contracts, or anything except the actual construction work out on the job.

Q. Well, buying pipe would be a part of the construction period, wouldn't it?

A. It would be part of that period, but not part of the construction work. I was referring to the actual time that we — spending money out on the job.

Q. There is no pipe on hand for a project such as the Chicago line, or this system, to be purchased, is there? That is, there is no pipe in stock?

A. Not such quantities as that, no, very small amount of pipe in stock.

Q. Has to be made specially by the mile, to fit the project?

A. In the Chicago line it was not only made, but there was nearly two years spent in the design of the pipe itself, and getting the pipe mills up to the point where they would make the pipe to withstand the pressures that were demanded.

Q. It was even necessary in some cases, was it not, for pipe manufacturers to build new mills to manufacture that pipe?

A. That was true, but away back of that was at least three years of time spent in getting the mills to even believe they could build the type of pipe we wanted.

Mr. Garver: I believe that is all.

Recross-examination.

Questions by Mr. Welch:

[fol. 529] Q. You say that you think it is more value to your company to be furnishing this gas to affiliated companies like the Kansas City, where they are controlled by the same company?

A. I think unless they should be controlled by another large holding company with ample facilities to go ahead and do the job as well as we think we can do it; in other words, at a time like this, if you had a small, isolated company to which you were supplying gas, and there was a question of extensions, it might not be able to raise the money.

Q. You are more friendly to the pipe line company than a foreign company would be?

A. No, a foreign company, if it is a large operating company, but an individual small company is often pressed by their necessities into an attitude that might not be to the best business principles.

Q. Isn't it true it would be more liable to pay you a little more for gas than it could get it for from some one else, if it is true the distribution company is owned by the same companies the pipe line companies are owned, wouldn't it be inclined to pay you a little bit higher price for gas than it could get it from someone else?

A. In the sense that they would not take up with a temporary supply and feel they could not get a permanent supply. Very naturally, since the preferred stocks are owned

by different companies that would have to do the best they could for themselves, we could not get ourselves in the position of penalizing the Kansas City Gas Company, for instance, with several millions of stocks and bonds owned by other people than ourselves, for the benefit of a company they only owned the common.

Q. I asked you whether you didn't think it would be inclined to take gas from you and pay you a higher rate than they could get gas from some other company.

A. No, I think they would be inclined to take gas from us on an equal basis.

Q. Now with reference to this pipe. you don't have to pay for the pipe when it is delivered, I take it that you pay for construction of the line?

A. That is true.

Q. So the fact that you had ordered your pipe sometime before the line was actually constructed, your cost of financing would not commence so far as your pipe was concerned, until you got your pipe.

A. No, that is perfectly true, but I was referring to cost of engineering and that sort of work that has to be done prior to placing orders.

Q. This preliminary engineering, of course, would have to be done in order to determine how much pipe you had?

A. That is true.

Q. I take it that is about the first thing you would do when you organized your concern, see whether it is feasible?

A. Yes, sir.

Q. And after that was done and you determined how much pipe you then ordered the pipe, it would be delivered, I suppose, as manufactured?

A. That is the way it was delivered.

Q. You would not have to wait for all the pipe for the system to be completed at the mill before you commenced construction of the plant?

A. No, you would not.

[fol. 530] Q. They would go ahead and manufacture a certain amount of it, and make delivery to you, probably make delivery to you as you needed it?

A. That is true, and the thing I had in the back of my head when I said fourteen months, I do not know that they averaged for that fourteen months, an expenditure of a

million dollars a week. That is what I had in mind, we were spending that money.

Q. You say we, who you mean?

A. I mean Henry L. Doherty & Company's people, because we were in the partnerships appointed to construct and have since been appointed to operate the line for the various partners in it.

Q. You are referring, then, to the construction of this Texhoma line to Chicago?

A. Yes, sir.

Mr. Garver:

Q. Mr. Hamilton, the practices of recognized engineers in valuing property have become very largely standardized, have they not?

A. To a very considerable degree, yes.

Mr. Garver: Properties have been valued for years for rate cases, and certain practices have developed?

A. Yes, sir.

Mr. Garver: Which are recognized, and there have been innumerable court decisions in regard to allowances for working capital, and going value?

A. Yes.

Mr. Garver: All those overhead items that you have used, have there not?

A. That is true.

Mr. Garver: Are the percentages which you have used in conformity with the generally recognized practice of engineers in valuing properties?

A. I should say so.

Mr. Garver: And with the decisions of the courts and commissions, generally?

A. Yes, sir.

By Mr. Welch:

Q. At any rate you think they are in accordance with the decisions of the courts?

A. I think that based on the cases in which I have been testifying, and in which the allowance have been made.

Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant, or something like that, there might be a wholly different basis.

Q. For instance you take the distribution plant, take the one here in Topeka, for example——

A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

A. That is true, and ten per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

A. That is true.

[fol. 531] Q. That should be taken into consideration in arriving at the going value in this case?

A. That is true.

Q. Then I take it you should take into consideration the fact here that the towns supplied by this pipe line company, with the exception of perhaps Superior, Nebraska, and those on the line west are accustomed to using natural gas, Kansas City, Topeka, Wichita, Ottawa, and towns of that kind have used natural gas for years, isn't that true?

A. That is what makes this pipe line valuable, because they have used it, and are in the habit of using it, and don't want to use anything else.

Q. And you should take into consideration that the building of this pipe line to those towns, those towns that already have been educated to be using natural gas?

A. You should not take it into consideration when you are arriving at a going concern value, no, sir, because that is what makes the going concern value.

Q. Well, if it does make it it should be taken into consideration?

A. Yes, sir.

Q. I thought you said it should not be?

A. It should not be to reduce it, because it makes the going value.

Q. Q. You mean to say it should not be taken into consideration to make it less?

A. I make a distinction between that and a town which had not been using gas, after you get it up to normal consumption.

Q. Then I understand in arriving at this going value, when you furnish gas to a distributing company that is in a town that has never used gas before, you say in cases of that kind there is a period of time before the people will be educated to using gas, and therefore if they are now educated to using gas, your going value should be that much more, is that the idea?

A. No, it should be the same in both towns after they get up to the normal use of gas. Now at the time the pipe line is first constructed to new towns that have not used gas, its going value would be less during those years, while they were getting up and getting into that condition of carrying the full load.

Q. The cost of attaching the business, if you supplied that gas to a company in a town where they are already educated to taking gas, it would not take so long there, and the expense of acquiring the business would not be near as much?

A. If you could presuppose some other pipe line had been supplying this town with gas, and today they could cut off and tomorrow we go on, it wouldn't take any time, but that isn't the conditions under which pipe lines are built. * * *"

"Eastman testified as to the Amarillo line from Texas to Wichita and Ottawa:

'Q. Now this line was built to Texas, was any addition to the market procured from that line, were any additional markets procured, any new customers? Are there any connected to that line between Texas and Wichita?

'A. No new cities, there may be a few small towns along that main line served, but they are inconsequential.

'Q. Was there any other purpose than to supply existing markets?

'A. No.'

"Eastman testified that the line from Ottawa to Kansas City was finished in 1929.

[fol. 532] "In January, 1930, from the 18th to the 19th, the pipeline's capacity was exceeded and it was necessary to shut off the industrial gas in order to supply the demand for domestic gas.

"Hamilton testified the third line was built from Ottawa to Kansas City to take care — increased capacity there.

"Jarboe testified further that the lines to the Amarillo, Oklahoma City and Seminole fields are purely extensions to procure additional supply. No new customers were added, just went to take care of the market.

"At the time of the purchase of the Kansas Natural, the personnel was retained and continued their work. There was a demand for the gas line from Wichita to Texas, the Amarillo line. The same is true with reference to all the additions put on to the old system.

'Q. As I understand it each one of them was built because there was a need and it was necessary to complete this, to furnish gas to the main pipe line, or to places where it had already contracted or made arrangements to sell gas?

A. One or the other.

Q. That is correct?

A. Yes.

Q. Each one of those red lines denoting the construction of new pipe lines was built by the Cities Service in order to fill a need that existed at that time?

A. Yes.

Q. Upon their being completed they were then immediately put in use?

A. Yes.

Q. And have been in use and operation since then?

A. Yes.'"

[fol. 533] Gas Leases

The following agreed statement was submitted to the District Court as evidence pertaining to Gas Leases:

"The company owned as of September 1, 1931, gas leases covering 1,262,361 acres of land situated in Kansas, Oklahoma, Missouri and Texas.

"These leases grant to the lessee the right to drill for and take oil and gas, and generally (with some exceptions), run for a period of ten years from date, after which, if oil or gas is not then being produced they expire, otherwise they run so long as oil or gas is produced. The leases in general require the payment of rental until development and require the lessee, after development, to pay to lessors a royalty of one-eighth of the oil and gas. The Company

owns only the gas rights in these leases, the oil rights being held in most cases by affiliated companies.

"These leases have been classified into developed, proven, probable and prospective.

" 'Developed' leases are those on which gas is actually being produced.

" 'Proven' are those adjacent to production, which will be drilled and on which it is considered gas will be found.

" 'Probable' consists of acreage adjacent to proven acreage having favorable geological structure, but which has not been completely tested.

" 'Prospective' consist of all other acreage.

" 'The acreage owned by the company, and appellee's classification of them is as follows (Ex. 40):

| [fol. 534] | Developed | Proven | Probable | Prospective, A | Total |
|---|---|---|---|---|---|
| Texas | 22,690 | 73,730 | 24,547 | ..... | 119,367 |
| Hugoton (Kan. & Okla.) | ..... | 123,440 | ..... | ..... | 123,440 |
| Okla., Kan. & Mo. | 20,207 | ..... | 1,060 | ..... | 21,267 |
| Okla., Kan. & Texas | ..... | ..... | ..... | 998,287 | 998,287 |
| | 42,297 | 196,170 | 25,607 | 998,287 | 1,262,361 |

"The same leases (excluding the Kansas, Oklahoma and Missouri, proven and probable) are classified by F. G. Holl, for the Commission, as follows:

Amarillo Field

| Proved Area: | Acres | |
|---|---|---|
| Blocked | 60,940 | |
| Unblocked | 33,767 | |
| Total | | 94,707 |

Hugoton Field

| Proved Area: | Acres | |
|---|---|---|
| Blocked | 25,280 | |
| Unblocked | 59,087 | |
| Total | 84,367 | |
| Probable or semi-proved areas | 32,008 | |
| Total | 116,375 | 116,375 |

Kansas, Oklahoma, Texas and Missouri.

| | Acres | |
|---|---|---|
| Favorable Acreage: | | |
| Kansas | 132,202 | |
| Oklahoma | 91,317 | |
| Texas | 36,326 | |
| Missouri | 9,064 | |
| Total | | 268,909 |
| Prospective Acreage: | | |
| Kansas | 364,669 | |
| Oklahoma | 248,208 | |
| Texas | 3,203 | |
| Total | | 616,073 |
| No value for gas: | | |
| Texas | 10,569 | |
| Oklahoma | 26,408 | |
| Kansas | 80,090 | |
| Total | | 117,094 |
| Grand Total | | 1,223,178 |

[fol. 335] Appellees contend that the fair value of these leases, exclusive of the wells and equipment, is $12,914,189.00, as follows:

All Cities Service Gas Company Acreage Average Value Shown by Appellee's Witnesses

| Name of field | Acres proven | Acres probable | Acres prospective | Total | Value per acre. |
|---|---|---|---|---|---|
| Amarillo | 94,820 | | | $8,879,628 | $93.64 plus |
| | | 24,547 | | 422,367 | 17.20 plus |
| Hugoton | 123,440 | | | 1,172,680 | 9.50 |
| All other | 20,207 | | | 377,940 | 10.70 plus |
| | | 1,060 | | 65,000 | 61.32 plus |
| | | | 908,287 | 1,996,574 | 2.00 |
| Grand total | 238,867 | 25,607 | 908,287 | $12,914,189 | |

[fol. 336] The several witnesses for the Company testifying as to the present fair market value of leases with respect to their experience and qualifications testified as follows:

J. N. Nisbet: That he is Chief Geologist of the Empire Companies including the Cities Service Gas Company; that he graduated from Leland Stanford University in

1916; that since 1916 he has had experience as a geologist over the entire mid-continent area particularly in Kansas, Oklahoma, Texas, Louisiana, Arkansas and New Mexico; that he has occupied his present position a little less than three years; that he is generally familiar with the prices that have been paid for leases in the Amarillo Field during the last five or ten years; that he is familiar with the present market value of acreage in that locality; that the prices testified to by him are not figured on the amount of gas under the ground and the market for such gas but what the present market is for the several leases; that his testimony is based on the study he has made of the field and his knowledge of exchanges and sales that have actually taken place; that he is familiar with the transactions that have taken place in the Hugoton Field and with the present market value of acreage in that field; that he is familiar with the present market value of acreage such as is owned by the company outside of the Amarillo and Hugoton Field.

Richard T. Lyons: That he is Vice President of the Skelley Oil Company and in charge of the Division of Lands and Leases; that he has occupied that position slightly over two years; that he has had twelve years' experience in the oil and gas business prior to the last two years; that he has supervised all lease purchases and sales by the Skelley Oil Company in the last two years; that his company has purchased and sold leases in the Amarillo Field during the last two years; that he is familiar with some of the transactions in the purchase and sale of leases [fol. 537] in that field in the last two years; that he is familiar with the present market value of leases in the Amarillo Field; that he is familiar with the present market value of leases in the Hugoton Field; that his company has bought acreage in that field; that his company owns acreage scattered all over the Amarillo Field comprising approximately 50,000 acres; that his company also owns acreage in the Hugoton Field, practically all of which was acquired in April, May and June of 1930.

B. A. Hardey: That he is an oil and gas operator connected with Moody Seagraves interests and Vice-President

of several of their companies; that he is familiar with the Hugoton Gas Field since April, 1929; that companies with which he is connected own approximately 450,000 acres of leases in that field; that all of this acreage was purchased since April, 1929, and that he is familiar with these purchases as all leases were taken either by him personally or under his supervision; that he follows rather carefully the transactions of all other companies in that field; that he is familiar with the present fair market value of leases in that field; that his testimony as to present market prices is based on his own purchases and observations of purchases made by others.

J. D. FREEMAN: That he is in charge of the geological and land and lease work for the Panhandle Eastern Pipe Line Company; that he is an engineer and not a geologist; that he has been in the gas business since 1903; that he is familiar with the Amarillo Gas Field; that he is familiar with purchases and sales that have taken place in that field in the last few years and under his direction purchased acreage for his company; that his company has about 70,000 acres in the Amarillo field; that the last leases he purchased were in March and April, 1931.

[fol. 538] A. W. LEONARD: That he is Vice-President of the Panhandle Eastern Pipe Line Company and has had thirty-five years' experience in the gas business; that he is neither an engineer or a geologist but connected with the Operating Department; that he went with his present company in October, 1930; that he is familiar with the purchases of gas acreage made by his company in the Amarillo Field, the last of which was purchased in August and September, 1930.

STANLEY MARSH: That he trades in oil and gas leases and oil and gas properties, his office being in Amarillo, Texas; that he has been acquainted with the Amarillo Field five years and has been engaged in the lease brokerage business in that field for four or five years; that he is familiar with most of the transactions that have taken place in the field; that he is familiar with the present market value of leases in the Amarillo Field.

VICTOR A. HAYES: That he has spent over thirty years in the natural gas business and has been associated with many different companies; that he has been familiar with the Amarillo Gas Field since 1924 and watched it from the beginning; that for the past four and a half years he was General Manager for the Southwestern Development Company and purchased their large holdings of acreage in that field; that he is familiar with the present market value of gas acreage in that field; that the last purchases he made were within six or eight months, the purchase consisting of 2,700 acres.

R. J. WALLACE: That he is in the brokerage business at Tulsa, Oklahoma, and has been for about six years; that in connection with his business he has kept himself informed as to the value of acreage in the Amarillo Field and is familiar with present market values.

[fol. 539] ROSS M. STUNTZ: That he is Superintendent of Gas Production for the Cities Service Gas Company; that he has been in the gas business practically all of the time since 1905; that all gas purchase contracts for the Cities Service Gas Company pass through his Department and are subject to his supervision and that he is familiar with the prices paid by the Cities Service Gas Company for all gas leases held by it and with sales and exchanges that have taken place in the several fields within recent years.

R. E. DAVIS: That he lives in Pittsburgh, Pennsylvania, and is a Consulting Geological Engineer; that his principal office is in Pittsburgh with some offices in New York, Charleston, West Virginia, and Shreveport, Louisiana; that he has been in such business twenty-five years; that all of his time for the last twenty-five years has been given to oil and gas work; that his firm has examined one or several times every important gas field in the country; that quite a large part of his work has been done for operating companies; that this is his first employment by any of the parties to this suit; that he was not employed to price the gas reserves of the Cities Service Gas Company but to value them; that his estimate is that of intrinsic value and not market price; that he determined his value in the same manner as if he were

employed by a client who was contemplating buying or a banker desiring to approve securities.

Davis testified that he did not attempt to ascertain market values or attempt to price the gas reserves of the Cities Service Gas Company in that manner but made a valuation by computing the amount of gas in reserve in accordance with the recognized practices of the industry and testified that, in his opinion, the value of the gas reserves, as a whole, was $20,588,000.00, including wells, the witness further testi- [fol. 540] fied that if the value of gas reserves, exclusive of wells, is to be determined the value found for the wells should be excluded from the above figure. (In Finding 14 the Court found the value of these wells to be $1,953,149.00 which would leave the value of the gas reserves, as testified to by Davis, $18,634,851.00).

Davis testified that in making his valuation he followed exactly the same procedure as if he were employed by any other client such as a banker or prospective purchaser and that the value testified to by him was the value he would use in such case.

Davis testified that he arrived at the intrinsic value of the proven and probable leases included in the above valuation by calculating the volume of the recoverable gas from these leases, and multiplying this by his estimated prices per 1000 c. f. of gas at the mouth of the well.

The testimony of these witnesses as to the present fair market value of the gas leases of the Cities Service Gas Company is set out in Exhibit 40, as follows:

[fol. 541]

All Cities Service Gas Company Acreage

Average market value as testified

| Name of field | Proven | | Probable | | Prospective | | Grand totals | |
|---|---|---|---|---|---|---|---|---|
| | Acres | Value | Acres | Value | Acres | Value | Acres | Value |
| Amarillo | 94,820 | 8,879,628 | 24,547 | 422,367 | | | 119,367 | 9,301,995 |
| Hugoton | 123,440 | 1,172,680 | | | | | 123,440 | 1,172,680 |
| All Other | 20,207 | 377,940 | 1,060 | 65,000 | 998,287 | 1,996,574 | 1,019,554 | 2,439,514 |
| Grand total | 238,467 | 10,430,248 | 25,607 | 487,367 | 998,287 | 1,996,574 | 1,262,361 | 13,914,189 |

(Vol. 642)

Estimate Book

| Tenancy of | | Present | | | | Previous | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Page | Acres | Price | Value | Page | Acres | Price | Value |
| J. M. Nisbet | | 387 | 34 2251 | 100 | £ 992 100 | 271 | 11 1491 | 25 | 365 100 |
| A. W. Tennant | Blocked | 388 | 10 2251 | 100 | £ 1 100 | 273 | 34 2251 | 25 | 862 100 |
| | Scattered | 388 | 6 1000 | 45 | 257 100 | 273 | | | |
| | Total | | 34 2251 | | £ 1259 100 | | | | |
| J. D. Freeman | Blocked | 390 | 10 2251 | 100 | £ 1 100 | 390 | 23 2251 | 24 | 565 100 |
| | Scattered | 390 | 6 1000 | 57 | 342 100 | | | | |
| | | | 34 2251 | | £ 1259 100 | | | | |
| R. T. Lyons | | 434 | 34 2251 | 75 | £ 1 100 | | | | |
| Stanley March | Blocked | 437 | 32 3000 | 225 | £ 1 100 | 440 | 1 1000 | 22 | 25 100 |
| | Scattered | 437 | 2 1000 | 75 | 1 100 | | | | |
| | | 437 | 34 3251 | 45 | 127 100 | | | | |
| | Total | | 34 2251 | | £ 1 100 | | | | |
| Victor A. Hayes | Blocked | 341 | 10 2251 | 100 | £ 1 100 | | | | |
| | Tenant's average | | 6 1000 | | 258 125 | | | | |
| | Total | | 34 2251 | | £ 1 125 | | | | |
| R. J. Wallace | Blocked | 392 | 10 2251 | 100 | £ 1 100 | 392 | 11 1491 | 13 | 145 100 |
| | Scattered | 392 | 6 1000 | 75 | 345 100 | | | | |
| | Total | | 34 2251 | | £ 1 100 | | | | |
| R. M. Stuntz | Blocked | 393 | 10 2251 | 100 | £ 1 100 | 393 | 34 3501 | 11 | 145 100 |
| | Scattered | | 6 1000 | 50 | 258 100 | | | | |
| | Total | | 34 2251 | | £ 1 100 | | | | |
| Grand Total | | | | | £ 137 125 | | | | |
| Average Total | | | 34 2251 | | £ 1 129 | | 34 3457 | | £ 1 |
| Average per Acre | | | | | 18 4 | | | | |

Ital 6481

Kingston Field

Person

| Testimony of | Page | Acres | Price | Value |
|---|---|---|---|---|
| J M Nesbit | 999 | 128,441 | 10 00 | 1,284,400 00 |
| H A Hardy | 472 | 128,441 | 10 00 | 1,284,400 00 |
| J H Freeman | 001 | 128,441 | 10 00 | 1,284,400 00 |
| H T Lyons | 005 | 128,441 | 8 00 | 987,528 00 |
| Average Total | | | | 1,172,682 50 |
| Average per acre | | | | 9 00 |

[fol. 544]

All Other Fields

| | Proven | | | | Probable | | | | Prospective | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Testimony of | Page | Acres | Price | Value | Page | Acres | Price | Value | Page | Acres | Price | Value |
| J. M. Nesbit | .... | | | | | | | | 379 | 1,005,194 | 2.00 | 2,010,388.00 |
| R. T. Lyons | .... | | | | | | | | 427 | 1,005,194 | 2.00 | 2,010,388.00 |
| R. M. Stuntz | | | | | | | | | | | | |
| Kansas | 917 | 16,125 | | 139,240.00 | | | | | | | | |
| Okla. & Mo. | 917-9 | 4,082 | | 239,700 | | | | | | | | |
| Total | .... | 20,207 | | 377,940 | 935 | 1,000 | | 15,000.00 | | | | |

[fol. 545] Computation for Prospective Acreage

| | | |
|---|---|---|
| Total Proven Amarillo | 94820 | |
| Total Probable Amarillo | 24547 | |
| Total Proven Hugoton | 123440 | |
| Total Proven all other fields | 20207 | |
| Total Probable all other fields | 1060 | |
| Total | 264074 | |
| Prospective | 998287 Acres @ 2.00 | $1,996,574.00 |
| Grand Total | 1262361 | |

[fol. 546] "These witnesses varied in their opinions of value of different tracts, the average of their testimony as to the present fair market value of all acreage being $12,914,189.00.

"The only witness testifying for the Public Service Commission was F. G. Holl, employed by it to value the gas leases of the Cities Service Gas Company, who testified as to his experience and qualifications as follows:

Direct examination:

"'A. Since January, 1919, I have devoted all of my time to the oil and gas business in varying activities. I commenced as a roustabout on a lease, dressed tools, and after about a year I was employed by the Empire Gas & Fuel Company in their geological department. My employment with them lasted over a period of almost six years. During more than a year of that time I was resident geologist for that company at Duncan, Oklahoma, and during the last three and a half years of that time I was resident geologist for the company at Eldorado, Kansas. As resident geologist, my work had to do with location of wells, drilling well, collection of data, and samples, geological work relating to these activities to some extent, examination of wildcat territory, recommendations on acquisition of acreage, and on rental payments. After leaving the Empire Company, in April of 1923, I was employed by the Ramsey Petroleum Company, of Eldorado, Kansas, for a period of one year. During that time, as their geologist, my work had to do with exploration, and during that period the Company acquired acreage and drilled wells and since April, 1926, I have been a consulting geologist and independent operator.' In P. 1878.

"I have bought, sold and developed oil and gas leases. I am familiar with the Amarillo and Hugoton fields. I have personally inspected and made a study of these fields. The market price for gas in the wells in the Amarillo field is 2 cents per M. c. f. I know the fair market value of oil and gas leases, insofar as there is any market value in these fields.

Cross-examination:

That he was 34 years old, and was not a college graduate and had no scientific degree; that after leaving school where he studied some geology he was employed by the Empire Gas & Fuel Company in September, 1919, in the so-called subsurface branch of the geologist department at Oil Hill; that he worked under H. R. Shidell, resident [fol. 547] geologist who reported to A. W. McCoy, who in turn reported to L. C. Snyder, chief geologist, at Bartlesville; that he had nothing to do with the purchase of leases; that his next position was with the same company at Duncan, Oklahoma, where there was an oil and gas field; that his duties at Duncan consisted of writing recommendations as to the location of both oil and gas wells; that he was in charge of geological office at Duncan; that he had no final judgment in regard to any matters; that he was given the responsibility of determining the point at which the casing should be set on rotary drill holes; that he kept track of the log of wells and ran samples; that all he had to do with the acquistion of leases was suggestions and recommendations in his reports; that in 1922, he was transferred from Duncan to Oil Hill, Kansas, as resident geologist; that in the course of his duties he made numerous recommendations chiefly in regard to construction work; that he was sent practically all over the state to make special reports; that he never worked in the land and lease department and never purchased but one lease for the company; that it was part of his duties to suggest leases for the company to drill on and the company drilled these leases; that he occupied that position three and one-half years, after which he went with the Ramsey Petroleum Company at Eldorado; that he personally handled over three or four thousand acres of oil leases purchased for that company; that he did no gas work for that company; that he occupied that position for a year and one month and then went into private practice as a consulting geologist.

"Q. Your qualifications as a consulting geologist at the time you opened your office were such as you have related up to this time, that was your experience, was it?

"A. Yes.

"Q. Are you still in that position?

"A. Yes.

"Q. You have been employed by the state to make a survey concerning which you have testified?

"A. Yes, sir.

"Q. It was 1926 you went into the business of a consulting geologist?

"A. Yes, sir.

"Q. Have you made any valuation of gas reserves for [fol. 548] any company since 1926, in the course of your business?

"A. I have made investigations.

"Q. Did any gas company, any oil company, any investment firm, any banker or any of the usual clients of that nature ever employ you to make an investigation and appraisal or valuation of a major oil or gas pool, the acreage of it?

"A. No, sir.

"Q. Prior to the time you were employed by the state in this case, had you made any such investigation or valuation anywhere, with the idea of fixing the value of leases?

"A. No. Prior to the time—you mean producing leases?

"Q. Yes, anything similar to what you are investigating now.

"A. Well, I think that most of my work has been of a similar nature.

"Q. Of a similar nature?

"A. Yes, sir.

"Q. For whom?

"A. For myself and for indepndent operators.

"Q. For what independent operator have you ever made an appraisal or valuation of gas reserves?

"A. I have made no such.

"Q. Well, when was your first experience with the Amarillo field, Mr. Holl?

"A. Since I was employed by the state.

"Q. You had no knowledge of the field prior to that time?

"A. Only a general knowledge from the literature which I had read on it.

"Q. You had never been down there and looked it over?

"A. Had not been until that time, no, sir.

"Q. What was your first experience with the Hugoton field?

"A. Two or three years ago.

"Q. That is when it first came in?

"A. Yes, sir.

"Q. Were you interested in it in the course of your business, or did you investigate it for some one?

"A. I was out there and investigated it for myself.

"Q. Just to satisfy yourself as to what there was out there as a matter of general information?

"A. Yes, and with the view of possible investments there.

"Q. Did you make any investments there?

"A. No, sir.

"Q. You stated that you were a geologist, and independent operator. What property have you operated? I am not going to inquire into your private affairs; it is not with that idea.

"A. I am not at this time operating any producing oil or gas leases which are operated by other companies.

"Q. Have you ever operated any oil or gas leases?

"A. I have drilled wells, if that constitutes operation.

"Q. Well, you have stated in the course of your employment you had done geological work, and you have drilled wells?

"A. Yes, and on my own account I have drilled wells.

"Q. As a driller?

"A. No, as an operator.

"Q. Now as to the Amarillo field, have you any independent knowledge of any transactions that have been taking place in the purchase or sale of leases?

"A. Yes, sir.

[fol. 549] "Q. You have never handled any such transaction yourself.

"A. No, I have not.

"Q. So what you know about it is what you have been told?

"A. Yes, sir, and what I have personally investigated.

"Q. What investigation did you make in the Amarillo field as the basis of your judgment as to the value of leases in that field?

"A. I familiarized myself with the lease situation there, prepared a map such as the map Exhibit G, and saw what acreage was leased to the different companies, pipe line companies, what acreage was either open or leased to oil

companies, or independent operators, I visited all the towns and county seats in the area, talked to bankers, abstractors, lease brokers, where there were any, visited all the principal offices in the Amarillo field, the oil and gas companies, talked with their geologists, land men and scouts.

"Q. That was to determine what acreage was good and what was bad, and the probable amount of gas in reserve, I take it?

"A. I wanted the information, all the information I could get from these men who were very familiar with conditions.

"Q. Did you ask them in regard to the market value, or price of acreage there, leases?

"A. Yes, sir.

"Q. Did you talk with the broker from Amarillo who testified in this case?

"A. Mr. Marsh?

"Q. Yes.

"A. Yes, I talked with Mr. Marsh.

"Q. Did the value he gave you correspond at all with the judgment you have now expressed?

"A. No, sir.

"Q. So you did not consider his judgment in the matter, did you, at all, did you tell these men that you talked to the nature of your employment and that you were representing the state in this proceeding?

"A. Yes, sir.

"Q. You didn't pose as a prospective purchaser trying to collect acreage, at all?

"A. Not to the men in Amarillo. * * *,"

"At the close of Holl's testimony before the Commission the respondents moved to strike out all the testimony given by him as follows:

"'* * * Mr. Garver: If the Commission please, the respondents and each of them, now move to strike from the record all of the testimony of Mr. Holl, in regard to the market value of leases in the Amarillo field, for the reason that he has not qualified himself as being able to testify to those values, inasmuch as he never operated in that field, was never in the field, and has no personal knowledge of any transaction that has taken place there, and never had anything whatever to do with the field until he was hired by the Commission, or by the state, to go down there and make an investigation, by reason of which fact he could

not know any more about it than any other person the Commission might have hired to go down there and make indiscriminate inquiries from anyone he might choose to pick out as to what the present market values were, his information being necessarily entirely hearsay, and the witness personally having no knowledge whatever of the market value of any leases in the Amarillo field of that vicinity. [fol. 550] I desire also to make the same motion as to the testimony of the witness in regard to lease values in the Hugoton field.

"Chairman Greenleaf: The motion will be overruled. * * *"

"The Commission found the fair value of these leases, exclusive of wells and equipment at $6,279,237.00, as follows:

Commission's Valuation of Gas Leases

| | Acres | | Value per acre | Fair Market Value |
|---|---|---|---|---|
| Amarillo field (Texas), Developed and Proven: | | | | |
| Blocked | 60,940 | @ | $50.00 | $3,047,000 |
| Not Blocked | 33,880 | @ | 35.00 | 1,185,800 |
| Total | 94,820* | | | $4,232,800 |
| Probable Acreage | 24,547 | @ | 2.00 | 49,094 |
| Total | 119,367 | | | $4,281,894 |
| Hugoton field (Kansas & Oklahoma), Proven: | | | | |
| Blocked | 25,280 | @ | $7.50 | $189,600 |
| Not Blocked | 59,087 | @ | 5.00 | 295,435 |
| Probable | 32,008 | @ | 2.00 | 64,016 |
| Total | 116,375 | | | |
| Prospective | 7,065 | @ | 1.00 | 7,065 |
| Total | 123,440 | | | $556,116 |

* Of the above, 22,090 acres are developed with sixty producing wells.

Kansas, Oklahoma, and Missouri (exclusive of Hugoton):

| | Acres | |
|---|---|---|
| Proven: | | |
| Kansas, Oklahoma and Missouri | 20,207 | $377,940 |
| Probable: | | |
| Kansas, Oklahoma and Missouri | 1,060 | 65,000 |
| Total | 21,267 | $442,940 |

| | Acres | |
|---|---|---|
| Prospective: | | |
| All other except Hugoton | 998,287 | 998,287 |
| Total | 1,262,361 | $6,279,237 |

[fol. 551] "In the foregoing, the Commission adopted the value of all the Kansas and Oklahoma (exclusive of Hugoton field) proven and probable leases, 21,267 acres, as claimed by respondents, at $442,940.

"The value of all leases of the company, including the leases later sold to The Texhoma after deducting the value of leases canceled and surrendered, as shown by the books of the company, is (book value) $6,573,489.70 (Tr. C. H. Montgomery, Ex. 49).

"Of the 1,262,361 acres of gas leases owned by the Company the Commission found that only 42,297 have been drilled or developed. The remaining 1,220,064 acres are undrilled and are undeveloped."

Amarillo Field (Texas).

"The company owns gas leases covering 94,820 acres in what is known as proven sweet gas area in Texas, in the Amarillo field. This proven sweet gas area is a portion of a huge field in the Panhandle, and is approximately 130 miles long and from seven to forty miles wide. It contains approximately 1,001,785 acres.

"Of the company's acreage in this field, the Commission found that 22,090 acres are developed, having sixty gas wells thereon. The testimony of Ralph E. Davis, the company's witness, a gas engineer and geologist, who made a survey of the company's gas holdings, is that the recoverable gas (gas reserves) from these leases situated in this proven area, and comprising 94,820 acres, is 15,000,000 cubic feet per acre.

"One of these Texas leases is the Burnett lease (Ex. 48). It covers 63,880 acres, and requires a minimum payment of $50,000 per year, in advance, for ten years whether or not gas is taken from the lease. For the first two years, the royalty is one-eighth of 3 cents per M. cubic feet for all gas taken; for the next three years, one-eighth of 3½ cents [fol. 552] per M. cubic feet; for the next five years, one-eighth of 4 cents per M. cubic feet; thereafter, one-eighth

of 4 cents unless the price of gas at the well is increased, in which event the royalty is to be one-eighth of the weighted average price. The Burnett lease is not a solid block, there being within said lease other leases owned by others than the company, on which there are producing wells. Up to the present time the $50,000 annual payments required on this lease have exceeded the royalty earned on the gas taken.

"The witnesses for the company placed the market value of these leases at from $45 to $125 per acre, the higher values being placed on the Burnett ranch and blocked acreage. Eight witnesses testified for the respondents, two of them were employees, and all of the remaining, save one, were connected with gas companies.

"F. G. Holl, for the Commission, testified that the value of the blocked acreage, consisting of 60,940 acres, was $45 per acre, and that the value of the remainder of the proven leases, 33,767 acres, was $25 per acre. Holl testified that scattered leases in this field in Wheeler County in the vicinity where the largest wells in the entire field have been found, could be purchased at $5 per acre, not to the purchaser, such leases covering both the oil and gas. That in Potter County, near where the largest wells have been found, on September 14, 1931, a lease which was about to expire was renewed at $8 per acre for 5,000 acres.

"The evidence of respondents shows in 1931 the company conveyed to the Texoma Natural Gas Company (an affiliated company) 59,788 acres of leases, including the Coon ranch of approximately 25,000 acres which was blocked, 30,831 acres at the price of $45 per acre and 28,957 acres at an average of approximately $19 per acre. This acreage was all in the proven sweet gas area in the Amarillo field, and Holl testified that these leases are comparable with the proven and developed leases retained and [fol. 553] now owned by the company. The evidence also shows that these leases so sold to the Texhoma cost the company somewhat less than $15 per acre on the average.

"The books of the company also show that from January 1, 1930, to June 30, 1931, it purchased 21,158 acres of its leases in the Amarillo field in the sweet proven gas area, now valued by respondents at approximately $93 per acre, at an average cost of $12.78 per acre.

"The evidence of Mr. Holl shows that there is a large oversupply of gas developed by gas companies and independent producers in the Amarillo field, which on account of the lack of market, cannot be sold, and that gas is being sold in this field at 2 cents per M. cubic feet, at the well. That in the Amarillo proven sweet gas area there are approximately 125 "shut-in" wells drilled and capable of producing gas which cannot be sold for want of a market, and that these "shut-in" wells have an open flow of 2,260,000,000 cubic feet per day.

"That the owners of wells are able to sell only a small per cent of their gas; that the Lone Star Gas Company has a pipe line into this field connected to 65 wells, from which the runs averaged during the first six months of 1931, a little over 100 M. cubic feet per day, for which the company paid 2 cents per M. cubic feet, or a royalty of $2 per day, and for that reason operators are not drilling any more wells or acquiring any more acreage.

"The company owns 24,547 acres of gas leases in Texas situated outside of the proven sweet gas area, some of which are in the sour gas area.

"The Testimony of the witnesses for respondents as to the value of this acreage varied. Some stated that part of these are worthless; others at from $5 to $25 per acre.

"F. G. Holl, for the Commission, placed the fair market value of the gas rights in that part of this acreage which is classed as "favorable" at $1 per acre and 50 cents per [fol. 554] acre for that part which he classes as "prospective" and nothing for the remainder of the non-producing Texas acreage.

"The Commission found the value of the gas leases in the Amarillo field as follows:

Amarillo Field

| Developed and proven: | Acres | Value per Acre | Fair Market Value |
|---|---|---|---|
| Blocked acreage | 60,940 | $50.00 | $3,047,000 |
| Not blocked | 33,880 | 35.00 | 1,185,800 |
| Total | 94,820 | ..... | $4,232,800 |
| Probable | 24,547 | 2.00 | 49,094 |
| Grand Total | 119,367 | ..... | $4,281,894 |

## Hugoton Field (Kansas and Oklahoma)

"The Company owns 123,440 acres of gas leases in the Hugoton field situated in northwestern Oklahoma and southwestern Kansas, all of which it contends are "proven".

"This is another enormous gas field estimated to comprise 1,000,000 acres of gas productive lands. Its limits are not yet defined. They can be determined only by additional drilling. Dr. Raymond C. Moore, State geologist, estimates the gas reserves in this field as sufficient to supply all of the state of Kansas, on the basis of that now used in Kansas, for a period of over 100 years (Tr. 1964, Ex. 47). There is a market for but a small portion of the developed gas in this field. Little drilling has been done, but there is sufficient drilling to demonstrate that this is a rich field of gigantic proportions.

"Of the company's acreage, F. G. Holl, for the Commission, classified 84,367 acres as "proven," 32,008 acres as "probable" and the remainder as "prospective."

"Ralph E. Davis, for respondents, gave it as his opinion, as a result of his geological survey made for respondents, that the recoverable gas from the "proven" area of this field is 10,000,000 cu. ft. per acre, and from the "probable" at 7,000,000 cu. ft. per acre.

[fol. 555] "There is no development and no wells on any of the company's acreage in the Hugoton field. The company's leases consist of one large lease, the Stonebreaker lease, covering 25,280 acres, and over 500 smaller leases. The terms of each of these 500 leases require the drilling of a well within ten years from its data, otherwise, the lease expires at the end of ten years. The company has no pipe line within ninety miles of these leases.

"Witnesses for respondents, four in number, testified that the fair market value of the gas rights in these leases which are in the proven area, is from $3 to $10 per acre, and the respondents claim that the fair market value of this 123,440 acres of leases is $1,172,680, or $9.50 per acre.

"F. G. Holl testified that leases for oil and gas could be purchased in the proven area of this field at the time of the hearing at $1 to $2 per acre; that the Derby Oil Company had within sixty to seventy days prior to his testimony,

purchased 5,947 acres of leases in this proven area at $1 per acre and that the fair market value of these leases is:

## Hugoton Field

Hugoton Field

| Proved area: | Acres | | Per Acre | Fair Market Value |
|---|---|---|---|---|
| Blocked | 25,289 | @ | $7.50 | $189,600.00 |
| Unblocked | 59,087 | @ | 4.50 | 88,630.50 |
| Probable area | 32,008 | @ | 1.00 | 32,008.00 |
| Prospective area | 7,065 | @ | .50 | 3,532.50 |
| Totals | 123,440 | | | $313,771.00 |

"The Commission found the value of the company leases in the Hugoton field to be $556,116.00, as follows:

## Fair Market Value Leases—Hugoton

Fair Market Value Leases—Hugoton

| | Acres | | Per Acre | Fair Market Value |
|---|---|---|---|---|
| Proven (blocked) | 25,280 | @ | $7.50 | $189,600.00 |
| Proven (not blocked) | 59,087 | @ | 5.00 | 295,435.00 |
| Probable | 32,008 | @ | 2.00 | 64,016.00 |
| Prospective | 7,065 | @ | 1.00 | 7,065.00 |
| Totals | 123,440 | | | $556,116.00 |

[fol. 556] Kansas, Oklahoma and Missouri (Exclusive of Hugoton Field)

## Proven and Probable

"Ross Stuntz, superintendent for the Company, testified that the company owned, in Kansas and Oklahoma, proven and developed and probable acreage, of the fair market value as follows:

| | Acres | | Fair Market Value | |
|---|---|---|---|---|
| Proven and developed: | | | | |
| Kansas | 16,125 | | $138,240 | |
| Oklahoma | 4,082 | | 239,700 | |
| Totals | | 20,207 | | $377,940 |
| Probable acreage: | | | | |
| Kansas | 80 | | $8,000 | |
| Oklahoma | 980 | | 57,000 | |
| Totals | | 1,060 | | $65,000 |
| | | 21,267 | | $442,940 |

"There was no other evidence as to the value of this acreage, and it was accepted by the Commission as correct.

## Prospective Acreage

"This acreage is scattered throughout Texas, Oklahoma, Kansas and Missouri.

"From July 1, 1931, to October 1, 1931, the company surrendered 61,471 acres of prospective acreage.

"The acreage of the company's prospective leases, as classified by Mr. Nisbet, chief geologist for respondents, is 998,287 acres, which he values at $2 per acre,

"Ralph E. Davis, for respondents, classifies 1,031,127 acres of the company's leases as "prospective" and values them at $1 per acre.

"F. G. Holl, for the commission, classified 268,909 acres, as "favorable" and values them at $1 per acre, 616,073 acres as "prospective" at 50 cents per acre, and the remainder at no value.

"The foregoing being for the gas rights only.

"The Commission found the value of this prospective [fol. 557] acreage to be $1 per acre, or a total of $998,287.00.

## Purchase Contracts and Gas Requirements

"The amount of gas produced and purchased by the company for the year ending December 31, 1930, is as follows:

| Gas purchased and produced: | M. C. F. |
|---|---|
| Gas produced | 34,401,978 |
| Gas purchased | 31,123,002 |
| Residue Gas purchased | 8,638,965 |
| Total | 74,163,945 |
| Or on an average per day of (74,163,945 + 365) | 203,189 |

"For the year ending June 30, 1932, the gas produced and purchased is as follows:

| | M. C. F. |
|---|---|
| Gas produced | 33,164,003 |
| Gas purchased | 14,848,685 |
| Residue Gas purchased | 6,608,886 |
| Total | 54,621,574 |
| Or on an average per day of (54,621,574 + 365) | 149,648 |

"This is an 8-oz. base, to reduce to a 2-lb. base, on which the measurement of the gas produced is based, this amount should be reduced by 9.2 per cent.

"The peak load of the company's gas system was on January 16, 1930. On that day the companies used 330,000 M. c. f. of gas.

"The pipe lines of the Company have no greater capacity than for this peak load.

"The Company has always purchased more gas than it produced. In 1930 it produced 46 per cent and purchased 54 per cent.

"The Company owns purchase contracts for gas on leases in the Kansas and Oklahoma fields adjacent to its pipe lines upon which are wells, the open flow production of which is 2,138,170 M. c. f. per day.

"These purchase contracts cover 782,421 acres of leases and 1,502 gas wells. The total open-flow capacity per day of the gas wells owned by the company, plus the gas to [fol. 558] which it is entitled under its purchase contracts, is: Open Flow per day:

| | M. C. F. |
|---|---|
| Amarillo, 60 wells, 22,090 acres (~~Tr.~~ 449) | 1,532,625 |
| Kansas, Okla. & Missouri, 20,207 acres (Ex. 3, Table 3) | 258,837 |
| Add purchase contracts (Ex. 3, 82-96, Tables 16 and 17) | 2,138,170 |
| Total open flow (available to company) | 3,929,632 |

"Respondents claim that the open-flow of the sixty wells in the Amarillo field is 250,000 M. c. f. less than the amount given above and if they are correct, the total open flow of gas available to the Company should be reduced to 3,679,632 M. c. f.

"The foregoing 3,929,632 M. c. f. is the open-flow capacity per day of the wells owend by the Company from 42,297 acres, all of its developed leases, plus the daily open-flow capacity of the wells situated on the leases covered by its purchase contracts.

"Witnesses testified that ordinarily the amount of gas which can be safely taken from a well is 20 percent of its open-flow capacity.

"The present maximum capacity of the company's pipe line from the Amarillo field, a 20-inch line, is 125,000 M. c. f. per day.

## Reserves

"Witnesses testified that the total acres of gas leases of the Company is 1,262,361. That of these, 22,090 acres in the Amarillo field and 20,207 acres in Kansas, Oklahoma and Missouri are drilled and producing and the remainder 1,220,064 were not drilled or producing or called upon at that time to meet the company's requirements for gas.

[fol. 559] "Ralph E. Davis, geologist and gas engineer, witness for the company, who made an exhaustive study of the company's holdings, testified that the recoverable gas reserves in the company's leases in the Amarillo field is 15,000,000 cu. ft. per acre for the proven and 7,500,000 cu. ft. for the probable. In the Hugoton field, 10,000,000 cu. ft. per acre for the proven and 7,000,000 cu. ft. per acre for the probable, and stated that these figures are conservative. Davis testified that the total amount of the developed acreage of the Company was 58,922 acres of which 19,882 acres were in Kansas, Oklahoma and Missouri and 39,040 acres were in Texas.

"That the total recoverable gas from companies' holdings in the Amarillo, Hugoton and Kansas, Oklahoma and Missouri leases, proven and probable, amount to 2,488,664,000 M. c. f. as follows:

| | Estimated gas reserves M cubic feet | Acreage |
|---|---|---|
| Kansas-Oklahoma (except Hugoton) and Missouri: | | |
| Proven, Developed | 23,858,000 | 19,882 |
| Probable | 9,566,000 | 1,020 |
| Total | 33,424,000 | 20,902 |
| Hugoton Field: | | |
| Proven | 492,100,000 | 49,210 |
| Probable | 196,490,000 | 28,070 |
| Total | 688,590,000 | 77,280 |

| Amarillo Field: | Estimated gas reserve M cubic feet | Acreage |
|---|---|---|
| Proven, Developed | 585,600,000 | 39,040 |
| Undeveloped | 836,700,000 | 55,780 |
| Total | 1,422,300,000 | 94,820 |
| Probable | 304,350,000 | 40,580 |
| Total | 1,726,650,000 | 135,400 |
| Grand Total | 2,448,664,000 | 233,582 |

"The Commission found that of the 1,262,361 acres of gas leases owned by the Company only 71,267 acres thereof were used and useful and devoted to the public use.
[fol. 560] "That included in these leases designated as "used and useful" are all of the developed leases in Texas, and all of the developed proven and probable leases (except Hugoton) in Kansas, Oklahoma and Missouri. A list of these leases with their recoverable gas reserves as testified by Ralph E. Davis, respondents' geologist and gas expert and their fair value as found by the Commission is as follows:

Used and Useful Leases, as Found by the Commission

| | Acres | Fair market value | Gas reserves M. c. f. |
|---|---|---|---|
| Kansas, Oklahoma & Missouri: | | | |
| All developed, proven and probable | 21,267 | $442,940 | 33,424,000 |
| Texas, Amarillo Field: | | | |
| Blocked | 45,830 @ $50 | 2,291,500 | |
| Not blocked | 4,170 @ $35 | 145,950 | 750,000,000 |
| Totals | 71,267 | $2,880,390 | 783,424,000 |

Of these 71,267 acres, 42,297 are producing and 28,970 acres are not developed, as follows:

| Proven Leases: | Acres |
|---|---|
| Developed: | |
| Texas | 22,090 |
| Kansas, Oklahoma & Missouri | 20,207 |
| Total | 42,297 |

| Undeveloped: | Acres | |
|---|---|---|
| Texas—proven | 27,910 | |
| Oklahoma—probable | 980 | |
| Kansas—probable | 80 | |
| Total | 28,970 | |
| Grand Total | | 71,267 |

"The gas reserve in these 71,267 acres according to respondent's testimony is 783,424,000 M. c. f.

"No witness testified that the leases other than the 71,267 acres were not used and useful.

"Respondents claim that all of the 1,262,361 acres of gas leases are used or useful.

[fol. 561] "The Commission found that only 71,267 acres of these leases are used and useful and rejects 1,191,094 acres as not devoted to the public use.

"Appellees value the 1,262,361 acres of leases at $12,914,189, exclusive of wells and equipment. The Commission valued these leases at $6,279,237—a difference of $6,634,952.

"Appellees value the 71,267 acres which the Commission found to be devoted to the public use at $5,124,940.

"The Commission values these leases at $2,874,390—a difference of $2,250,550.

It was agreed before the district court that the witness, F. G. Holl for the Commission, would testify "that he is familiar with the gas holdings of The City Service Gas Company, that he has made a study of them by inspection and by examination of the maps and data furnished by the Company and that he is familiar with the location of all wells owned by the Company in the Amarillo field. That he has made a calculation for the purpose of determing the amount of developed acreage owned by The City Service Gas Company as of September 1, 1931, and that in doing so he has used the following basis:

"In the case of scattered acreage he has considered that the wells situated on such scattered acreage develop the entire acreage owned by The City Service Gas Company surrounding said wells. In the case of blocked acreage he has assigned to one well, 640 acres surrounding said well, subtracting overlapping acreage due to the close spacing of wells. That from an examination of the maps furnished

by the Company showing location of wells and acreage owned, he has determined that the amount of scattered acreage, that is acreage that is not blocked, in the Amarillo field is 10,110 acres having 39 wells thereon, and that the blocked acreage is 11,980 acres, having 21 wells thereon, and that through this calculation he finds that the total developed [fol. 562] acreage of The City Service Gas Company in the Amarillo field is 22,090 acres.

"That in arriving at the developed acreage situated in Kansas and Oklahoma, he has accepted the classifications of Ralph E. Davis, geologist introduced as a witness for the company, and his written report classifying said acreage being Exhibit #3, page 36. That according to this classification, the remainder of all of the developed acreage of The City Service Gas Company is 19,882 acres. That including the developed acreage outside of the Amarillo field with that in the Amarillo field, the total developed acreage of The City Service Gas Company, as of September 1, 1931, is 41,972 acres.

"That the total number of wells owned by the City Service Gas Company as of September 1, 1931, is as follows:

| | |
|---|---|
| Amarillo field | 60 |
| Kansas & Oklahoma producing | 147 |
| Storage | 66 |
| Dead | 31 |
| Total wells | 304 |

"That in accordance with the records of the Railroad Commission of the State of Texas, there are at the present time in the so-called West Panhandle (Amarillo) field, 56 gas wells which are shut in and have no market for their gas. These wells have an open flow per day of 1,467,600,000 cubic feet and are situated within from one-fourth mile to five miles of The City Service line, 19 of them being within one mile of the City Service line.

"That during the year, 1932, a new field of gas has been opened in Reno County, Kansas, within approximately 28 miles from Wichita, Kansas, and 12 miles from Hutchison, Kansas, and within 3 miles of The City Service 10-inch line. That the open flow capacity of these wells at the present time is approximately 270,000,000 cubic feet per day. That

the limits of the field are not yet determined. That the City Service pipe line has recently been connected with two [fol. 563] of the wells in this field whose open flow capacity is approximately 146,000,000 cubic feet of gas per day.

"It is contended by the Complainants that the 270,000,000 cubic feet above mentioned is sour or sulphur gas and not yet proven to be useable by The Cities Service Gas Company.

"It is agreed that the book value of the leases of the Company, after deducting the cost of the leases transferred to the Texoma, is $5,727,272.00.

"Exhibit 3, pp. 20-26, prepared by Ralph E. Davis, for the Company, shows that on July 1, 1931, the Company had 147 producing gas wells and 66 storage and 31 dead wells on 19,882 acres of leases in Kansas and Oklahoma, and 60 producing wells in the Amarillo Texas field. Said Exhibit 3, Table 10, shows the amount of gas produced and purchased in M cubic feet on an 8 oz. pressure basis for the years 1927 to 1930 and six months of the year, 1931, as follows:

Cities Service Gas Company, Cities Service Gas Pipe Line Company, American Pipe Line Company

Gas Produced and Purchased

M Cubic Feet—8 oz. Pressure Base

| | | Kansas | Missouri | Oklahoma | Texas | Total |
|---|---|---|---|---|---|---|
| 1927 | Gas Produced | 525.809 | | 2.286.173 | | 2.811.982 |
| | Gas Purchased | 8.386.761 | | 19.268.498 | | 27.655.259 |
| | Residue Gas | 737.878 | | 14.345.453 | | 15.083.331 |
| | Total | 9.650.448 | | 35.900.124 | | 45.550.572 |
| 1928 | Gas Produced | 1.615.217 | | 3.694.818 | 10.272.560 | 15.582.596 |
| | Gas Purchased | 7.423.485 | 409.829 | 18.671.840 | 15.121 | 26.520.275 |
| | Residue Gas | 1.445.867 | | 12.962.828 | | 14.[illegible].696 |
| | Total | 10.484.569 | 409.829 | 35.319.486 | 10.287.681 | 56.501.565 |
| 1929 | Gas Produced | 1.343.788 | 6.643 | 4.564.662 | 28.230.126 | 34.145.219 |
| | Gas Purchased | 8.687.833 | 989.257 | 19.332.388 | 913.063 | 29.922.541 |
| | Residue Gas | 360.381 | | 7.871.587 | | 8.231.968 |
| [fol. 564] | Total | 10.392.002 | 996.900 | 31.768.637 | 29.143.189 | 71.299.728 |
| 1930 | Gas Produced | 1.054.074 | 10.847 | 3.548.557 | 29.788.500 | 34.401.978 |
| | Gas Purchased | 9.787.394 | 642.565 | 20.357.803 | 335.240 | 31.123.002 |
| | Residue Gas | 155.516 | | 8.483.449 | | 8.638.965 |
| | Total | 10.996.984 | 653.412 | 32.389.809 | 30.123.740 | 74.163.945 |
| 1931 | Gas Produced | 585.186 | 4.158 | 839.254 | 15.153.456 | 16.582.054 |
| 6 Mo., | Gas Purchased | 4.430.386 | 206.255 | 6.390.835 | 220.185 | 11.247.661 |
| | Residue Gas | 131.083 | | 6.586.581 | | 6.717.664 |
| | Total | 5.146.655 | 210.413 | 13.816.670 | 15.373.641 | 34.547.379 |

RALPH E. DAVIS, Gas Engineer and witness for the Company, testified:

In the Amarillo field the developed acreage is that part of the proven acreage surrounding the various wells that have been drilled by the Company and I have arbitrarily assigned 640 acres to each well, that being based on the judgment that one well to each 640 acres would be economical and sound judgment. There are wells where you cannot get 640 acres around them. In that case, for example, where a well is drilled on an 80-acre tract I would let the well develop 80 acres. I would just take 80 acres as the amount developed in that case, that is all I would take.

Wells are spaced according to a wide variety of conditions. The outline of lease boundaries, the size of a lease and many other features are factors that determine the number of wells to be drilled on any given area. Under normal conditions a well producing from a sand formation will drain from 30 to 80 acres. Wells producing from porous limestone, as in the Amarillo field and the Hugoton field, will drain considerably more than that.

Some of the lease owned by the Company in Texas are outside of the sweet proven area and are in the sour gas area. I classified 10,680 acres in the Amarillo field as sour gas.

Sour gas is not suitable for domestic consumption.

I have valued the prospective acreage of the Company, Kansas, 597,919 acres, Oklahoma, 410,469 acres, Missouri, [fol. 565] 8,799 acres, and Texas, 13,940 acres, at One Dollar per acre.

In Carson County, Texas, in the Amarillo field the rock pressure of the wells has dropped in three and one-half years from 412 to 406 pounds, and during that time the wells have produced 69,996,000,000 cu. ft. of gas.

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J. M. NESBIT, Chief Geologist and witness for the Company, testified:

The conferences for the sale of the 59,786 acreage of leases which were transferred to the Texoma, as of August 1, 1931, occurred in the year, 1930. Some of these leases which were afterwards transferred were acquired by the

Company in 1928. Along with the gas leases were transferred nine gas wells. The profit on the sale of these leases was in excess of One Million dollars, and on the sale of the gas wells was $11,000.00.

The number of gas leases held by the Company is approximately 7,000.

During the period from July 1, 1931, to November 1, 1931, the Company surrendered 61,471 acres of its gas leases as of not sufficient value to warrant the payment of rental.

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Ross Stuntz, Superintendent of Production, witness for the company, testified:

The capacity of the pipe lines connected with the leases covered by purchase contracts is less than the amount of gas obtainable from the purchase contracts and said pipe lines are not sufficient to carry all of the gas available from these gas leases.

That in the year 1927 the Cities Service Gas Company produced only about 10% of the gas required for its system and purchased the balance; that at the present time (1931) in the month of June, the company produced 44% of its gas and purchased 56%; that the gas available under gas purchase contracts is not sufficient to take care of the peak demands of the company in winter; that the entire gas reserves of the company were bought for the sole purpose of assuring the gas supply and not for speculation and that, in his opinion all of such reserves are necessary for such [fol. 566] purposes.

The witness further testified that during winter peak demands it is necessary to turn in all wells connected to the system, whether owned by the company or under purchase contracts, and that under such conditions said wells, as a whole, on the average are capable of delivering only approximately 12% of their open flow; that during the winter of 1930 (the winter preceding the hearing) all the gas available to the system was necessary for service; that the Amarillo line was delivering 100,000,000 cubic feet a day, its full capacity, into the system and that without that line the system would have been 100,000,000 cubic feet per day short and that service would have failed; that there is

no gas purchased on the Amarillo line, all being gas owned and produced by the company.

[fol. 567] Mr. H. L. Eastman, Engineer and witness for the Company testified:

That the Amarillo line had at times been out of service, both from accident and for repairs, and the Company was able to maintain its service so that its customers knew nothing about it.

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On September 6, 1932, the Railroad Commission of Texas made the following order:

"Oil and Gas Docket No. 108

In re Conservation and Prevention of Waste of Crude Petroleum and Natural Gas in the Panhandle District

Austin, Texas, September 6, 1932.

Whereas, as public hearings at Pampa, Texas, on July 16, 1932, in Austin, Texas, on August 10, 1932, and in Amarillo, Texas, on September 1, 1932, after due notice, further testimony was heard with respect to waste of gas in the Panhandle Field; the control of the production and transportation of gas in such field; and with respect to the applications of Hagy, Harrington & Marsh, and others, to utilize the so called 'dry gas' produced from the West Panhandle Gas Field for the extraction of gasoline; and

Whereas, it appears that in the West Panhandle Gas Field, herein defined as the present producing sweet gas area and extensions thereof, in Moore, Potter, Hartley, Oldham, Hutchinson, Carson and that part of Gray County, Texas, embraced in Block 3, I. & G. N. Survey and Block B-2, H. & G. N. Survey, there exists an area comprising all that portion of the sweet gas area in Blocks 3, 4, and 7, I. & G. N. Surveys, and Block B-2, H. & G. N. Survey, Carson and Gray Counties, Texas, located east of a line drawn north and south through the southeast corner of Section 14, said Block 7, and the northeast corner of Section 116, said Block 4, in which there are some thirty-one (31) wells

which have been closed in for some time because there has been no market outlet for the gas, nevertheless in said area there are many wells which are producing gas inasmuch as the owners thereof have a market; and

Whereas, a Three Judge Federal Court, by opinion filed June 8, 1932, in what are generally known as the Common Purchaser Gas Cases, held that the statutes of Texas and orders of the Railroad Commission of Texas issued thereunder are void insofar as they undertake to compel gas pipe line companies to become common purchasers of gas under the provisions of the Common Purchaser Act; and

Whereas, beyond question the wells producing gas are draining gas from the properties upon which wells have been completed but have no market outlet, and will continue to so drain such properties, as well as others upon which no wells have been drilled and are not being drilled because no market exists for the gas; and

Whereas, the restriction of the use of such gas for light or fuel will result in confiscation of the gas of many lessees and its appropriation by those having a market outlet, unless, under Article 6008 of the Revised Statutes of Texas as amended, permits be granted for the use of such gas for other purposes than light or fuel; and

Whereas, The Attorney General, by opinion dated July 7, 1932, has ruled that, under certain circumstances, the granting of such permits would be conducive to the public welfare as contemplated by said Article 6008; and

[Fol. 5058] Whereas, Hugy, Harrington & Marsh and others have filed applications for the right to use gas produced from their wells in the area mentioned for the extraction of gasoline, and proof has been made that there is no reasonable prospect of finding a market for such gas,



for light or fuel, and consequently confiscation of their properties will take place if the use of gas be so restricted; and

Whereas, others similarly situated have informed the Railroad Commission of Texas that they will file similar applications for permits to extract gasoline from so-called 'dry gas'; and

Whereas, conditions with respect to drainage are particularly serious in the eastern portion of said West Panhandle Gas Field, as particularly described in the second paragraph hereof, and the owners of leases which have no market outlet are insisting that permits for extraction of gasoline be granted without delay unless ratable marketing of gas be obtained or some other means be adopted to prevent drainage of their properties; and

Whereas, those pipe line companies controlling the market outlet for gas refuse to purchase ratable and to take any gas except from their own wells, and, under said Federal Court decree, this Commission has been enjoined from enforcing the provisions of the Common Purchaser Act and must, therefore, if confiscation be prevented, either grant the application to extract gasoline from the gas, with the consequent loss of the residue and tremendous physical waste, or else prevent drainage and resulting appropriation by closing down all wells where drainage would be immediately affected, as in the area described in paragraph second above, and by requiring ratable production from other wells in the field;

Now, therefore, be it ordered that:

(1) All gas wells in the area last described in paragraph second above be closed in until such time as the owners of the wells in such area have a market which will insure ratable production, and outlet.

(2) Each well in the balance of the West Panhandle Gas Field being all of the field except the eastern portion as described in paragraph second above, from which gas is being used for light or fuel, shall be restricted to a flow of not more than 4% of its potential capacity, or so much of such potential capacity as may be necessary to take care of current demand for domestic and industrial uses.

(3) Wells in the West Panhandle Gas Field from which gas is being used for light or fuel in nearby towns are expected from subdivision one (1) of this order, on the ground of public necessity, pending further consideration of the facts to determine whether such wells can also be shut in.

Railroad Commission of Texas."

Later the Cities Service Gas Company, and others, brought suit to enjoin the enforcement of said order before a Three-Judge Court on the ground that the same was unconstitutional. Thereafter, the Railroad Commission rescinded said order, pending the determination of the constitutionality of said order.

## Affidavit

The following affidavits were submitted by plaintiffs at the hearing before the 3-Judge Court:

[fol. 569] "H. R. STRAIGHT, of lawful age, being first duly sworn, upon oath, says: that he is now and for 17 years last past has been a resident of Bartlesville, Oklahoma; that he majored in Economics and graduated from Leland Standford University, a duly accredited college. That his occupation during said time has been carrying on the work of oil and gas business, including companies handling by-products of said substances and business similar to said business. That for the last ten or twelve years he has been the General Manager of Cities Service Gas Company and/or its predecessor companies. That in addition to his education along lines of the petroleum industry, affiant has had actual experience in the drilling of and supervising of drilling of oil and gas wells in Pennsylvania and other eastern fields for a period of about twenty years and approximately nineteen years in the Mid-Continent oil and gas area. That by virtue of his experiences and study of the Mid-Continent oil and gas region he had become familiar with the oil and gas fields in the states of Oklahoma, Kansas, Texas, New Mexico, Arkansas and Louisiana. That he is familiar with the experiences of the Kansas Natural Gas Company, The Wichita Gas Company, The Wichita Pipe Line Company and the Quapaw Gas Company from approximately the time such companies began to do business until their property was acquired by the Empire Natural Gas Company the predecessor of Cities Service Gas Company. That most of the difficulties of said companies arose or became acute largely because of frequent shortages of an adequate supply of gas or their difficulty in obtaining such supply.

Affiant further says that it is often impossible even with the aid of the most experienced and best qualified experts

to accurately forecast the existence, extent or durability of a gas field at any given place, and by reason of such fact any gas company that keeps abreast of usual competition must constantly keep a large reserve of gas acreage. That plaintiff and or its predecessor companies, during his knowledge of them, has always attempted to keep a sufficient gas reserve to insure dependable service to its patrons and has practically always been successful in so doing since the experiences of shortage of gas above alluded to occurred. That in said effort to constantly insure adequate gas reserves the plaintiff has at times had a far greater amount of acreage available to it than it now possesses and has uniformly found constant preserving of ample reserves [fol. 570] was advantageous. By reason of such policy, plaintiff has gradually built up a reputation for unexcelled service in the gas business.

Affiant says that for a long time past and now, the Cities Service Gas Company has acquired its gas reserves and acreage after exhaustive research; and as to the propriety and profitableness of the respective portions from time to time considered, and the acquisition of additional acreage from time to time, it is always a subject of serious consideration, conferences and exchange of ideas among its managing agents before such additional acreage is acquired. That in the judgment of affiant it is not only proper but reasonably necessary that plaintiff have for the business it conducts the gas acreage and reserves that it now possesses and such was the deliberate business judgment of the various managing agents who have collaborated with him in reaching the decisions from time to time to acquire such acreage.

Affiant further says that plaintiff does not now, nor has not for a number of years, owned any gas reserves or gas leases that are, or have been acquired for the purpose of sale, or are, or were held for speculation. That all the gas acreage that it now owns was acquired and is held by the plaintiff for the purpose of ensuring an adequate supply of gas to its patrons.

That plaintiff has but one single business, which is the business of supplying gas to its patrons through its network of pipe lines lying in the States of Texas, Oklahoma, Kansas, Nebraska and Missouri, which gas it wholesales to its customers; that it currently receives no income except

that produced from said business; that unless it uses a portion of the income from said business to maintain and preserve its leasehold estates, acreages and gas reserves, same will be lost to it and plaintiff will not be able to continue in the future to have a dependable gas supply that it customarily possesses nor give that dependable service which it has uniformly given to its patrons."

"George H. Band, of lawful age, being first duly sworn upon his oath says: That he is now and for the last sixteen years has been a resident of Bartlesville, Oklahoma; that by profession he is a mechanical engineer. That he is a graduate of the State Agricultural College, now known as Kansas State College, at Manhattan, Kansas, a duly accredited college, in which he majored in mechanical engineering and from which he duly graduated as a mechanical engineer in 1914. That thereafter he was employed by the [fol. 571] Westinghouse Electric Company at Pittsburgh, Pennsylvania, until he took employment with a predecessor in interest of the Cities Service Gas Company. That he has occupied positions in practically all branches of the field work pertaining to the production, transportation, sale and delivery of natural gas having successively been a field man, a meter man, superintendent of meters, conductor of industrial sales, and is now and for some time last past has been General Superintendent of operations over the whole system of Cities Service Gas Company located in the States of Texas, Oklahoma, Kansas, Nebraska and Missouri.

Affiant says that he is thoroughly familiar with all the pipelines, compressor stations and other equipment for transporting and delivering gas in said system. That in the usual course of his work it has become necessary for him to familiarize himself with the present fields of gas supply and to take part in all the conferences of executives and operatives in planning for the procuring of adequate gas reserves and the extensions of pipelines to the vicinity of such reserves not only for the dependable service of existing markets and utilization of the present sources of supply, but for the prevention of future shortages and the solving of problems that from time to time confront plaintiff in the expansion of its business and the consequent increase of reserves and equipment to accomplish and pro-

tpot such expansions. That he believes he is thoroughly familiar in a general way with all of the mechanical and operative problems that have in the past few years confronted plaintiff and which naturally will arise in the near future.

That plaintiff produces or buys, transports and sells at wholesale natural gas in quantities ranging from a minimum of about 100,000,000 cubic feet of gas a day to a maximum of about 330,000,000 cubic feet of gas a day. That a large portion of said gas is sold for domestic or heating purposes concerning which there is a high seasonal fluctuation and large daily and hourly variation. On account of this fact, among other things, it is necessary for plaintiff at all times to have large and dependable gas reserved and large pipeline capacity and a large number of compressor stations with separate units of power that may be thrown into or out of use upon short notice and to have more or less of a network of lines so that in case of breakage or washouts or other similar impediments the gas flowing in one portion of said system may be propelled to any other portion of the system desired.

[fol. 572] That about five years ago, plaintiff acquired a large gas reserve in the State of Texas and caused to be built to it a twenty inch pipeline, the maximum capacity of which is about 125,000,000 cubic feet of natural gas daily. That about the same time it caused to be built a sixteen inch pipeline for the purpose of conveying gas from what is known as the Seminole Field of Southern Oklahoma. That shortly thereafter it built a twenty inch pipeline from what is known as the Oklahoma City Field northward to the proximity of Wichita, Kansas. That shortly after the completion of said large trunk lines leading from its gas reserves it made eastern extensions to its existing gas pipeline system, one from the northern part extending a distance of approximately 110 miles from Ottawa, Kansas, to Sedalia, Missouri, and consisting of a twelve inch pipeline of the approximate ultimate capacity of 50,000,000 cubic feet of natural gas daily, together with an eight inch extension northward therefrom about 44 miles to the vicinity of Carrollton, Missouri; another extension being an eight inch line from Petrolia, Kansas, to the vicinity of Fort Scott, with facilities on eastward to the vicinity of Nevada, Missouri; the third extension being from a point a short

distance south of the City of Joplin, Missouri, eastward about 75 miles to the City of Springfield, Missouri, and consisting of a ten inch pipeline of the approximate ultimate capacity of 25,000,000 cubic feet of natural gas daily.

That it is and has been for many years last past the custom of plaintiff to frequently hold conferences not only upon present problems, but to estimate and figure out the probable future contingencies and problems that will arise in the usual course of its business. That in the remote past plaintiff has had unfortunate and costly experiences because of lack of adequate gas supplies and reserves for pipeline capacity, arising partly because of premature and unexpected exhaustion and depletion of gas reserves partly on account of breakage of lines with inadequate auxiliary equipment to serve during the respective emergencies. On account of this experience this affiant and the executives of plaintiff have become familiar with the perplexing and costly problems that arise because of not having reserve line capacity and gas supply, and in the recent years last past have sought to so amplify their line capacity and gas supply and reserves that it may at all times furnish a dependable gas supply to the customers who serve the greater [fol. 573] part of the State of Kansas and a large part of the State of Missouri. To obtain a satisfactory degree of dependability it has been necessary for plaintiff for many years past, and is now necessary for it, to have large natural gas reserves located in as diverse directions from the center of its system as is practical and with the view of preserving a dependable supply at the lowest cost it acquired large supplies or reserves in the Seminole Field, the Oklahoma City Field, the Texas Panhandle Field, the Oklahoma Panhandle Field, the Hugoton Field, other Western Kansas Fields, and Northeastern Oklahoma. That the acquisition of these respective supplies and reserves has been a matter of serious consideration by the meeting of managers of plaintiff for the past several years and no supplies or reserves are ever acquired except after a deliberate decision by its managing agents that they are necessary for the dependable operation of the only business conducted by the plaintiff, which is that of gas producing, transporting, selling and delivering which is carried on through its integrated pipeline system in the aforesaid states. That plaintiff has no other business than the said

business and has acquired no gas acreage for any other purpose than for the serving of said business, and does not now and has not in the recent past acquired any gas acreage for speculative purposes or to sell to others.

That plaintiff at all times employs and uses in its customary and ordinary course of business a large staff of expert and experienced geologists who continuously by use of maps and all the other paraphernalia known to petroleum geologists attempt to analyze and delimit the known developed fields and also to discover and demonstrate the productivity of other areas not now developed or used for gas production. That notwithstanding the large experience of affiant and the managers of plaintiff and the assistance of the geological staff mentioned it is not always possible for plaintiff to foretell the extent or productivity of areas examined and analyzed or of new fields. That if plaintiff should wait for the discovery and development of new fields by others it would probably frequently experience shortages of supplies necessary for its markets while so waiting for others to take the lead, and also if plaintiff should abjure all initiative on its part and wait for others to develop gas fields it would be compelled to pay exorbitant prices for its gas reserves and supplies and at times be confronted with the alternative of either paying pro-
[fol. 574] hibitive prices or being short of gas. That in acquiring new acreage plaintiff gives great consideration to the proximity of same to its present or projected lines and practically all of plaintiff's gas acreage, amounting to about one and one quarter million acres, is located within practical striking distance of present or prospective lines.

That plaintiff ordinarily considers the building of large trunk lines over periods varying from one to five or more years in advance of the time they are built. That the Seminole line was a piecemeal construction, section of same being build progressively as fields from which it served were discovered, the last section of which was considered about two years before same was built. The Oklahoma City line was under consideration for approximately two years before it was built. The Texas Panhandle line was under consideration about five years before it was built. Plaintiff is now and for about two years last past has been considering the building of a line from the Hugoton Field of Kansas and Oklahoma to join with its system in the

vicinity of Wichita, Kansas, and to run through the large acreage of plaintiff intervening between the termini of said line.

That on account of the eastern extension aforesaid into Northwestern, Western and Southwestern Missouri, plaintiff has very little surplus line capacity during normal times and considering normal peaks. If the markets along the Sedalia, Nevada and Springfield lines develop in the proportion that new fields or markets normally develop, plaintiff's line capacity and compressor station capacity will shortly become inadequate. That because of said extensions being so new affiant believes that the markets along same will radically increase and that much more gas will be necessary to be carried through said lines. That recently the Railroad Commission of Texas issued and served upon plaintiff an order requiring it to shut down twenty three of its gas wells in the Panhandle of Texas and limiting the production of the remainder of its gas wells in the Texas Panhandle to four per cent of their respective open flows. That the said gas wells have an average open flow of approximately 20,000,000 cubic feet daily. That if said order be continued in operation it will prevent plaintiff from taking more than 32,000,000 cubic feet of gas daily from the Texas Panhandle, whereas the capacity of its said Texas Panhandle line is approximately 125,000,000 cubic feet and it is accustomed at peak times to use it to near its capacity. By reason of said order and while it continues [fol. 575] in force plaintiff will be compelled to procure from 50,000,000 to 100,000,000 cubic feet of gas from other sources and through other channels than those now in use, and plaintiff will be compelled to develop and use gas reserves not now developed and in all probability will be compelled to resort to its holdings in the Hugoton Field in Kansas and Oklahoma. That on account of the Missouri extensions mentioned it has already enlarged constrictions in its Southern Kansas trunk line and Quapaw line from twelve inches to sixteen inches thereby giving to plaintiff more line capacity to said Missouri markets. That on account of said extensions into Missouri and the said consequent enlargements plaintiff has been, and is holding the Hogshooter compressor station in constant readiness to serve its said pipeline systems and especially its said extensions into Missouri. That by use of said compressor

station it would add a transmission capacity of approximately 20,000,000 cubic feet of natural gas daily and by such use it can accomplish such result much cheaper than in any other manner. That while said order of the said Texas Railroad Commission is operative it will be necessary for plaintiff in cold weather to use said Hogshooter compressor station to increase the transmission capacity of its lines from whatsoever source it gets its added gas supplies, and whether said Texas order remains in force or not upon resumption of normal financial conditions or the natural growth of the Missouri markets along the said newly constructed extensions the economical operation of plaintiff's system will require the operation of the Hogshooter compressor station. That when the said Hugoton line is built this will add greatly to the supply of gas that can be delivered at Wichita; but to transmit said gas to our eastern extension lines or other markets east of Wichita it will be necessary to add additional expensive compressor units and probably to build additional transmission line capacity. However, by the use of Hogshooter station and the use of the Southwestern portion of plaintiff's pipeline capacity it can increase the volume of gas for delivery to said eastern extensions and the markets north of Ottawa by approximately 20,000,000 cubic feet daily. That until it becomes imperative to build the Hugoton line to add gas supplies for plaintiff's markets, as aforesaid, it would be much more economical to strengthen the transmission power of the southeastern portion of plaintiff's pipeline system and use the Hogshooter compressor station, and this is the course that it is the present intention of plaintiff to pursue. [fol. 576] That the said strengthening of the transmission power of the southeastern portion of said system will not permanently solve the question confronting plaintiff as to the increase of the transmission power of its entire system, but the use of the Hugoton Field in Kansas and Oklahoma is bound to become necessary in the not far distant future in the ordinary course of the business of said plaintiff."

"H. L. Montgomery, of lawful age, being first duly sworn upon oath, says that he is now and for thirteen years last past has been a resident of Bartlesville, Oklahoma, and during the last ten years of said time has been the Manager of Cities Service Gas Company and its predecessor com-

ponent companies; that he is now and for several years past also been Vice President of Cities Service Gas Company. That in the performance of his duties as such Manager he has become familiar with the prices charged for natural gas by our pipe line companies in Kansas and other adjoining states, and is familiar with the prices charged by plaintiff in all States in which it operates and is in a general way familiar with the distributing companies that purchase gas in said States and their respective corporate affiliation.

Affiant further says, that plaintiff is now and has been for many years last past selling Domestic gas in Kansas at the respective City Gates of the distributing companies which purchase from it at approximately the rate of forty (40) cents per thousand cubic feet, except that it is and has been thus selling to distributing companies located in the proximity of what is known as the "Southern Kansas Trunk Lines" at the approximate rate of thirty eight (38) cents per thousand cubic feet. That plaintiff does not now and never has made any differentiation whatever as to price between sales made to distributing companies that were affiliated with it and sales made to unrelated distributing companies on account of the existence or lack of corporate relationship. That where conditions are essentially similar it is now and has been in the past selling gas to affiliated companies at the same rate at which it sells to unrelated companies. That a tabulation truly showing its sales to unrelated distributing companies in the State of Kansas giving rate per thousand cubic feet, number of customers and approximate population in the different towns is hereto attached marked Exhibit "A" and made a part thereof. That a tabulation truly showing its sales to unrelated distri- [fol. 577] bution companies in the State of Missouri, giving rate, per thousand cubic feet, number of customers and approximate population of the respective towns, is hereto attached and marked Exhibit "B", and made a part hereof. That a tabulation truly showing contract for sales to companies that were unrelated to plaintiff at the time the contracts were made, but are now owned by companies affiliated with plaintiff, giving rate per thousand cubic feet, number of customers and approximate population of respective towns, is hereto attached marked Exhibit "C" and made a part hereof. That several of the unrelated companies to

which plaintiff sells gas are adjacent to or within striking distance of other large gas pipe lines and practically all of the unrelated companies to which plaintiff sells are either near said large pipelines or smaller pipe lines, which more clearly appears from a map showing pipeline system of plaintiff and that of other large pipelines near said unrelated markets which is marked Exhibit "D" and made a part hereof.

That the City Gate rate of forty (40) cents was fixed by the Public Utilities Commission of the State of Kansas, the predecessor of the said Public Service Commission, in 1923 and was decreed by said Commission at said time, composed of C. M. Reed, H. A. Russell and J. W. Greenleaf as Commissioners, to be the reasonable City Gate rate for main line gas except as to said Southern Kansas Trunk Line for which it was decreed by said Commission the thirty eight (38) cent City Gate rate was the reasonable price. That so far as Affiant is informed no application to said Public Utilities Commission, or Public Service Commission of Kansas, has been made by citizens in the towns affected for the lowering of the Gate rate prices so fixed as aforesaid.

That affiant is familiar with the establishment and growth of the component companies that entered into the formation of Empire Natural Gas Company now known as Cities Service Gas Company. That said component lines were built piece meal from time to time to reach markets progressively acquired and in the fields of supply necessary to be reached.

That at the respective times during which those pipelines were thus intermittently contracted, the distributing companies now receiving gas from Cities Service Gas Com- [fol. 578] pany were not owned by Cities Service Gas Company, and for the most part at the time the contracts for the sale of gas at the City Gates were made were not owned by or affiliated with any of the pipeline companies which were brought together to compose plaintiff's present intergrated system of pipelines.

Affiant says that the domestic rate charged by plaintiff in Kansas is in line with, or lower than the rates charged by comparable pipe line systems under similar circumstances. That the usual Gate rate price of Panhandle and Eastern corporations where taken from the Texas Panhandle and Hugoton field is through Kansas into Missouri is in said

States approximately forty (40) cents per thousand cubic feet. That the usual City Gate price of the Community Natural Gas Company, a subsidiary of the Lone Star Gas Company, so far as it pertains to sales in Oklahoma, is approximately forty five (45) cents per thousand cubic feet. That the schedule of rates of the Natural Gas Company of America which takes gas from the Panhandle of Texas through the intervening States to a point near Joliet, Illinois, their sales, some wholesale, if applied to the load factors existing in the markets of plaintiff in Kansas, would be considerably higher than those charged by the plaintiff in Kansas. That about ten days ago the Public Utilities Commission of Ohio fixed as the reasonable City Gate rate for the Ohio Fuel Gas Company to charge to the distributing companies of Columbus, Ohio, rate of thirty nine (39) cents per thousand cubic feet. And affiant further says, that the distance from the place of production of the gas to the city of Columbus is very much less than the distance from plaintiff's greatest source of supply to its largest markets.

Affiant further says that on account of the experiences of its predecessor component companies in the past as to gas shortages, the necessity of maintaining at all times an ample and dependable gas reserve has been strongly impressed upon affiant and the officers and directors of Cities Service Gas Company, and they have without raising the aforesaid Gate rate, acquired large and dependable gas reserves, acquisition of which was the result of the deliberate judgment of the directors and officers of plaintiff, including this affiant; that it was necessary to have and continuously maintain the present gas reserves or gas reserves of similar extent and dependability.

That it is very desirable to have gas reserves located in [fol. 579] as diverse a direction from the geographical center of plaintiff's system and markets as possible, and plaintiff's gas reserves have been acquired largely with relation to its markets and its existing or projected pipe lines and the respective capacities of such pipe lines. That within the last five or six years plaintiff has made enormous investments in additional pipe line and transportation facilities in order to utilize its gas reserves and ensure a stable and dependable supply to its customers and to keep pace with the growth of its markets, not only in its new extensions into the State of Missouri, but also into the State of Kansas,

and during such period it has not raised, nor sought to raise the City gate rate fixed as aforesaid by said Commission."

Exhibit "A"

Foreign Distribution Properties Served by Cities Service Gas Company, Kansas

| Community | Company | (1930 census) population | 1-1-32 customers | Town border rate domestic |
|---|---|---|---|---|
| Altamont | American Gas Co. | 598 | 215 | 38¢ M. c. f. |
| Anthony | Western Natural Gas Co. | 2,497 | 466 | 40¢ " |
| Atchison | Kansas Power & Light Co. | 13,034 | 2,500 | 40¢ " |
| Bassett | Allen County Supply Co. | 104 | 60 | 30¢ " |
| Baxter Springs | Baxter Springs Gas Co. | 4,541 | 993 | 38¢ " |
| Cherokee | American Gas Co. | 1,158 | 147 | 38¢ " |
| Clearwater | United Gas Service Co. | 981 | 133 | 40¢ " |
| Columbus | American Gas Co. | 3,235 | 704 | 38¢ " |
| Conway Springs | United Gas Service Co. | 981 | 183 | 40¢ " |
| Emporia | Kansas Electric Power | 14,007 | 2,743 | 40¢ " |
| Galena | American Gas Co. | 4,730 | 623 | 38¢ " |
| Harper | United Gas Service Co. | 1,485 | 245 | 40¢ " |
| Lawrence | Kansas Public Service | 13,726 | 4,241 | 40¢ " |
| Leavenworth | Kansas Electric Power Co. | 17,466 | 3,357 | 40¢ " |
| Lebo | Ross Gault | 500 | 70 | 40¢ " |
| Lyndon | United Gas Service Co. | 742 | 69 | 40¢ " |
| Melvern | United Gas Service Co. | 445 | 55 | 40¢ " |
| Oswego | American Gas Co. | 1,845 | 407 | 38¢ " |
| Quenemo | United Gas Service Co. | 564 | 94 | 40¢ " |
| Scammon | American Gas Co. | 1,093 | 131 | 38¢ " |
| Thayer* | United Gas Service Co. | 495 | 140 | 30¢ " |
| Treece | Baxter Springs Gas Co. | 740 | 47 | 38¢ " |
| Wellington* | Wellington Gas Co. | 7,405 | 2,012 | 10¢ " |
| Totals | | 92,755 | 19,406 | |

* Local Gas.

Exhibit "B"

Foreign Distribution Properties Served by Cities Service Gas Company, Missouri

| Community | Company | (1930 census) population | (1-1-32) customers | Town border rate domestic |
|---|---|---|---|---|
| Carl Junction | Carl Junction Gas Co. | 1,500 | 200 | 40¢ M. c. f. |
| Holden | Interstate Gas Co. | 1,807 | 127 | 40¢ " |
| Kingsville | Interstate Gas Co. | 237 | 21 | 40¢ " |
| Lexington | Missouri Gas & Electric Service Co. | 4,595 | 643 | 40¢ " |
| Marshall | Missouri Gas & Electric Service Co. | 8,103 | 881 | 40¢ " |
| Oronogo | Citizens Gas Co. | 575 | 115 | 40¢ " |
| Platte City | Missouri Gas & Electric Service Co. | 587 | 54 | 40¢ " |
| Pleasant Hill | Interstate Gas Co. | 2,330 | 243 | 40¢ " |
| Smithfield | Carl Junction Gas Co. | 150 | 20 | 40¢ " |
| Weston | Missouri Gas & Electric Service Co. | 1,028 | 90 | 40¢ " |
| Totals | | 20,912 | 2,405 | |

Exhibit "C"

Properties in Missouri Served by Cities Service Gas Company, Formerly Owned by Urban Service Company and Now the Property, Ozark Distributing Co. (Subs. of Gas Service Co.)

| Community | (1930 census) population | (1-1-32) customers | Town border rate domestic |
|---|---|---|---|
| Carrollton | 4,058 | 163 | 40¢ M c f |
| Concordia | 1,140 | 43 | 40¢ " |
| Norborne | 1,190 | 21 | 40¢ " |
| Sweet Springs | 1,641 | 76 | 40¢ " |
| Totals | 8,029 | 303 | |

Other towns included in contract between Urban Service Company and Cities Service Gas Company, but to which pipelines were never built are:

Fulton, Higginsville,
Glasgow, Hardin,
Fayette, Norborne
Slater,

all in Missouri.

The Springfield Gas & Electric Company serving Springfield, Missouri (Population 1930 Census 57,527, No. of customers 1-1-32, 7201) was a foreign distribution property when the contract was signed July 26, 1929, but has since become an affiliated company. The town border rate on domestic gas is 40¢ M c f.

## Depreciation of Overheads

The following was submitted to the District Court on depreciation of overheads:

"The following tabulation shows the amounts of overheads included in the valuations of Black and Hamilton, respectively, and the last column the allowances which were made by the Commission:

[fol. 581]

Undistributed Overheads Depreciated

| Item | Black | | Hamilton | | Commission | |
|---|---|---|---|---|---|---|
| | RCN | PV | RCN | PV | RCN | PV |
| Administration & Legal Expense | $1,287,348 | $1,144,475 | $348,586 | $348,586 | $340,094 | $304,084 |
| Taxes During Construction | 875,171 | 778,044 | 769,174 | 769,174 | 875,171 | 778,044 |
| Interest During Construction | 4,323,212 | 3,859,204 | 6,337,986 | 6,337,986 | 4,351,934 | 3,883,282 |
| Miscellaneous Construction Expense | | | 769,174 | 769,174 | 680,187 | 606,169 |
| Engineering & Supervision | 3,196,878 | 2,846,163 | 3,459,011 | 3,166,329 | 3,218,585 | 2,881,900 |
| Total | 9,682,609 | 8,627,889 | 11,719,931 | 11,427,249 | 9,465,971 | 8,454,579 |
| Reduction in Rate Base by Depreciation of Overheads other than Eng. & Supt. | | 704,905 | | | | 673,807 |
| Replacement Reserve Allowance @ 2.96% | | 280,605 | | 346,910 | | 280,193 |

[fol. 582] "These overheads were not depreciated by Hamilton with the exception of the item for engineering and supervision. The allowance for annual depreciation testified to by Eastman amounted to $3,276,325.07. Eastman unintentionally failed to make an allowance for depreciation on the item of Engineering and Superintendence. Engineering and Superintendence was included by Hamilton in the amount of $3,459,011.00 and the proper allowance for depreciation if the Hamilton valuation is adopted would be 2.96% of that amount or $102,387.00.

| | |
|---|---|
| Eastman's Exhibit No. 27 | $3,276,325.07 |
| Correction for Engineering & Superintendence | 102,387.00 |
| | $3,378,712.07 |

The allowance by the Commission for annual depreciation and depletion was $1,786,338.88. The Commission, as shown above, did deduct accrued depreciation from all of these overheads in arriving at the total value found. The Commission did not make any allowance in their annual depreciation computation for these items.

"If it is not proper to depreciate the overheads as shown in the above tabulation there should be added to the Commission's value the sum of $673,807.00 and if it is proper to depreciate them there should be added to replacement reserves on the basis of Black's value the sum of $286,605.00 and on the basis of Hamilton's value the sum of $346,910.00 and on the basis of the Commission's finding the sum of $280,193.00.

## Annual Depreciation and Depletion Requirements

The following agreed statement was submitted to the District Court on annual depreciation and depletion requirements:

"Under this heading in its opinion, beginning at page 110, the Commission discusses requirements for physical equipment other than gas leases, requirements pertaining to gas leases, general development expense capitalized, [fol. 583] amortization of non-producing leases, dry hole expense and annual requirements for depletion of producing leases. All of these matters will be considered under this heading.

"The only evidence in regard to replacement reserves covering all of these items was that of H. L. Eastman in support of his Exhibit 27 in which he set up reserves totaling $3,276,325.07 divided among the several accounts as appears by the exhibit, which is as follows:

| | |
|---|---|
| Production Field Measuring Stations | $41,635 |
| Production Other Structures & Equipment | 3,401 |
| Production Gas Well Construction & Equipment | 183,882 |
| Production Field Line Equipment | 322,492 |
| Production Drilling & Cleaning Equipment | 3,283 |
| Transmission Rights of Way | 91,183 |
| Transmission Other Structures | 4,884 |
| Transmission Measuring Stations | 45,491 |
| Transmission Compressing Station Structures | 76,682 |
| Transmission Compressing Station Equipment | 283,625 |
| Transmission Line Equipment | 1,103,071 |
| Transmission Other Equipment | 416 |
| General Other Structures | 3,657 |
| General Office Equipment | 10,782 |
| General Store Equipment | 169 |
| General Shop Equipment | 1,350 |
| General Stable Equipment | 54 |
| General Laboratory Equipment | 837 |
| General Tools & Implements | 5,136 |
| General Other Equipment | 1,525 |
| Sub-total | $2,183,555 |
| General Development Expense Capitalized | 532,530.77 |
| Amortization of non-Production Leases | 314,981.68 |
| Dry Hole Expense | 174,747.74 |
| Depletion of Producing Leases | 70,509.88 |
| Total | $3,276,325.07 |

In Exhibit 27 Eastman unintentionally omitted an annual allowance for the depreciation on engineering and superintendence. The Commission used an average of 2.96% for annual depreciation on all physical property, which is accepted by the parties. Applying this 2.96% to the

account of engineering and superintendence resulted in a figure of $102,387.00 which should be added to Mr. Eastman's total for replacement reserves of $3,276,325.07, making the total $3,378,712.07.

"The average of Eastman's allowance for replacement reserves, when applied to Hamilton's valuation of those accounts, results in an average per cent of 3.01, as appears in the opinion, page 111. The witness P. McDonald Biddison, testify for respondents, testified:

[fol. 584] 'I would say in general that a minimum rate of depreciation for any natural gas pipe line system would be 4%, and that in many cases it would have, if your fields are short lived, to be on up well above 4%.'

"The Commission calculated in per cents the replacement reserves testified to by Eastman as to the several accounts as applied to the value of the property found by Hamilton for the accounts respectively and arrived at the several per cents set out in the table on pages 110 and 111 of the opinion. The application of these per cents to the several values found by the Commission resulted in an average per cent of 2.96 for all depreciation and amortization purposes, exclusive of leases.

"The Commission undertook to average replacement reserves requirements and found such requirements for the property in existence on September 1, 1931, to be $1,889,022.00; for the property in existence December 31, 1930, to be $1,693,312.00 and for the property in existence June 30, 1931, to be $1,712,216. The Commission then averaged the last two figures notwithstanding the fact that the two annual periods used by it were only six months apart and overlapped and arrived at an average figure of $1,702,764.00, which is the allowance made by the Commission for annual depreciation on physical property other than leases."

[fol. 585] "Amortization of non-Producing Leases"

Under this heading the Company seeks to include in its annual reserve allowance $314,981.68 for the amortization of non-producing leases, which is claimed as necessary to amortize the cost of leases owned by the Company which are

not producing. This figure of $314,981.68 is taken from the books and covers the experience of the Company for the year 1930 and includes amortization for the year 1930 on the non-producing leases sold to the Texhoma Company in the latter part of 1931.

General Development Expense

The company asks for an annual reserve allowance of $532,530 for general development expense capitalized.

Eastman testified that this item includes the following character of expenditures; Cost of acquiring leases; geological expense; lease rentals.

The cost of acquiring leases was made up of salaries and expenses of men engaged in acquiring leases and scouting expenses.

The item of $532,530 represents the expenditures for leasehold development charged to capital investment during 1930. This sum is also found on the last page of Eastman's Exhibit 8, which shows the "Net Additions to Plant and Investment" each year from 1923 to 1930, inclusive, and for the first six months of 1931, under the column headed "1930," and it was added to the plant investment account in the books in that year. It includes expenditures for development of leaseholds, consisting of cost of acquiring leases, geological costs, and lease rentals during that year incurred in part in connection with leaseholds and wells sold to the Texhoma Company during the latter part of 1931, and subsequently the Texhoma repaid this expense to the Cities Service Company. The above amount is estimated as the future annual expenses for leases for those purposes. These general development expenss are capitalized. Rentals on non-producing leases amounted to $329,917.00.

[fol. 586] "Dry Hole Expense"

The appellees asked for an annual allowance in the amount of $174,474.74 for dry hole expense. This is an amount which the Company seeks to have allowed as an annual allowance for expenses in drilling dry holes. This figure is based on the experience of the Company for the year 1930. In 1930, the Company drilled ten dry holes on scattered acreage in Oklahoma, Kansas and one well in

Texas, none of which was drilled upon the territory now designated as proven.

"The Commission adopted Hamilton's figure of $70,509.88 for depletion of producing leases. If this Commission's theory that non-producing leases should not be amortized is adopted, respondents contend that if all leases are found to be used or useful the allowance for depletion of producing leases of $70,509.88 should be increased in the sum of $314,981.68 to cover that portion of the cost of leases that has hitherto been amortized through the allowance of depreciation on non-productive leases and that if the Commission's theory that overheads should be depreciated is adopted there should be added to the Commission's allowance for replacement reserves the sum of $280,193.00 and to Hamilton's allowance the sum of $244,523.00, each figure being 2.96 per cent of the overheads included in the values respectively which have been depreciated by the Commission.

"In this connection Mr. Eastman testified as follows:

'Q. What is the last item we have here, depletion of producing leases?

'A. Depletion of producing leases is—represents that portion of the leases which have been depleted during the past year on account of the gas taken from that lease. * * *

* * * * * * *

'Q. Now how did you arrive at your figure of $70,509.88?

'A. I didn't arrive at that figure myself, it was calculated by our operating departments. * * * A. I didn't arrive at it. Those calculations are currently made by the operating department, based on geological information, and operating records. * * *"

[fol. 587] Net Income

It was agreed by the parties before the District Court that the net income of the Cities Service Gas Company, before depreciation and depletion and before adjustments for Henry L. Doherty & Company payments for the year ended December 31, 1930, was $8,829,480.71; for the year ended June 31, 1931, $8,741,809.14 and for the year ended June 30, 1932, $7,861,516.85.

Included in the expense for the year ended December 31, 1930, was an item of $75,022.33, representing payments

made to Henry L. Doherty & Company, which the Commission disallowed as an operating expense and added to the net income of the company for the year ended December 31, 1930.

Included in the expense for the year ended June 30, 1931, was an item of $68,882.05, representing payments made to Henry L. Doherty & Company, which the Commission disallowed as an operating expense and added it to the net income of the company for the year ended June 30, 1931.

Included in the expense for the year ended June 30, 1932, was an item of $52,297.13 representing payments made to Henry L. Doherty & Company, which the Commission disallowed and added to the net income of the company for the year ended June 30, 1932.

Included in the operating expense for the year ended June 30, 1932, was an item of $50,000.00 for the amortization of expense for the present investigation, which the Commission disallowed and added it to the net income for the year June 30, 1932.

"For the reasons stated in the opinion, the Commission also added to net income for each of the years ended December 31, 1930, and June 30, 1931, $78,874.00 because of the fact that no other figure appeared in the record. This addition is in error as the net income used by the Commission for the year ending December 31, 1930, in amount $8,829,480.71, included a construction credit for that period amounting to $118,488.75 and the net income used by the Commission for the year ending June 30, 1931, in amount $8,741,809.14, included construction credit for that period amounting to $114,118.00."

[fol. 588] Average Value During Period Covered by Earning Statement

The following agreed statement was the evidence submitted to the District Court on the average value during period covered by earning statement:

"Under this heading the Commission's opinion, pages 121 to 124, purports to set out values of the property as of September 1, 1931, July 1, 1931, January 1, 1931 and July 1, 1930, and from such values to determine an average value.

"The net additions to fixed capital tabulated on page 123 of the opinion were taken from the fixed capital account of

the Cities Service Gas Company by the Commission's auditor. Eastman testified that under the accounting practice of the company there was a lag between the time a line was completed and placed in operation and the time the job order was closed and posted to the fixed capital account of from one to three years and that therefore the fixed capital account did not reflect the total property of the company on the several dates used by the Commission.

[fol. 589] Eastman testified on cross-examination as follows:

"Q. Exhibit No. 88, which you referred to yesterday, was prepared from the books of your company as to unfinished construction?

"A. Yes, sir.

"Q. Now, as I understand from your explanation yesterday, the books did not reflect the actual situation as to unfinished construction?

"A. They reflect the actual situation as to uncompleted job orders, they do not as to the dates on which entry is made, the books reflect the actual time as to the construction of the property.

"Q. That is, you cannot refer to your books and find out whether construction is finished?

"A. Construction is finished, as I tried to explain——

"Q. I understand that it is done before it appears on the books, simply answer the question. I want to know if I am right on this, you cannot refer to your books and determine whether or not construction is completed and in use?

"A. Yes, sir, you can refer to the books——

"Q. What books?

"A. The same items you have here, because the construction is done before these entries are ever made.

"Q. Is the construction completed before the money is expended?

"A. The construction is completed at the same time the money is expended. The money is expended before it appears on the books.

"Q. Well, now, when a construction job is started and money is expended for labor or material, what entry is made upon the books of the company?

"A. That entry is made on the books at that time.

"Q. Where is that entry made, in what account?

"A. Well, it depends entirely on the nature of the construction as to what account it would be. The usual procedure on construction of any project, is for the construc[fol. 590] tion to be approved by means of what we term a requisition. The requisition is approved, authority given for proceeding with the construction work, a job order is opened, thereafter charges in connection with the construction are made to this job order.

"Q. That did I understand you to say the construction was completed before the entires were made on the books?

"A. In some cases, yes, in small jobs.

"Q. Well, on your large jobs, do you go ahead with construction and then expend the money?

"A. Yes.

"Q. That payment is then placed upon the books, isn't it?

"A. As the money is actually spent, yes, sir.

"Q. Then none of your larger construction would the construction be completed before the money was expended and placed upon the books?

"A. It might be, I did not say it would be.

"Q. That is some of your larger lines, you think the construction might be completed before the money was expended?

"A. No.

"Q. Well, before the money is expended

"A. Construction in that case will be completed before the final entries go on the books.

"Q. But the larger part of the entries should be there?

"A. I presume so, yes, on a large job.

"Q. Well, then it is impossible for us to determine from the examination of your books what construction was completed during the last 18 months?

"A. I believe that is generally correct, as I testified yesterday.

"Q. And it is impossible for us to determine from an examination of your books, what construction was incomplete on September 1st, and in operation?

"A. That is generally correct, yes, sir.

"Q. Well, then, Mr. Eastman——

"A. Probably true because of the law between the time the work is actually done and the entries being made on the books, because there is bound to be a certain lag in there, however, it is perfectly possible to tell by inspection of the property at any certain date what work is done.

[fol. 591] "Q. Take the Wichita compressor station, what would be the lag there?

"A. The lag in this case has been in the neighborhood of a year.

"Q. That is, the property was in operation a year before the entries were made?

"A. The exhibit which you have here lists uncompleted job orders as of June 30, 1931. The property actually went in operation in the fall of 1930.

"Q. Can you give us the dates on which these entries were made on the books?

"A. That varies almost from the time the work actually started, up until June 30, 1931, and possibly some since.

"Q. The items of expenditures were made, and were entered on the books?

"A. Yes.

"Q. There was no particular gap there, especially, of a year between the time the expenses were made and entered on the books, was there?

"A. There might be in case of disputed charges.

"Q. These would be very few, would they not?

"A. I think so.

"Q. In other words, Mr. Eastman, they take your book value then does not correctly reflect the value of the property in operation?

"A. No, sir, the book value does not reflect the value of the property in operation. We have made no such claim. I believe that was the purpose of Mr. Black making his appraisal, to determine the value of the property.

"Q. I mean, it does not reflect the actual cost?

"A. No, sir, there is always a lag.

"Q. Will you furnish to the commission the unfinished construction at the date September 1st, 1931; and also the construction which was finished and put in operation for an 18-months' period preceding that date?

[fol. 592] "Mr. Garver: I don't think we ought to go to that trouble and expense. Mr. Eastman knows personally these units are in operation.

"Mr. Hatcher: Your books don't reflect it and it is hard for us to get it.

"Mr. Garver: You are not accepting our books for that purpose. You won't take the book value of our plant ac-

count for this rate base, these items are all completed, Mr. Eastman has testified they are in his valuation and they are in Mr. Black's valuation, Mr. Black knows whether they are or not.

"Mr. Hatcher: I believe Mr. Eastman; he could not go through and give us the exact dates, there is no way the commission can know when this property was put in operation.

"Mr. Garver: You can analyze those job orders, why should we put in weeks doing it.

"Mr. Hatcher: We cannot analyze the job orders.

"Mr. Garver: A job covers $5,000,000, a contractor is paid a monthly statement of cost on the job order and when the payment is completed

"Mr. Hatcher: That does not tell us when the property went into operation.

"Mr. Garver: It is all in this valuation.

"The Witness: I think Mr. Black can identify practically every bit of that property, being in his valuation.

"Mr. Hatcher: Was not used and useful, covered by the period covered by his valuation?

"A. It certainly was. I testified it was in operation.

"Q. Will you furnish us that information?

"A. No, sir; I won't.

"Q. Will you furnish it, Judge Garver?

[fol. 343] "Mr. Garver: No, I don't think we should be asked to go to that expense. If anybody wants to go to the trouble of analyzing out these job orders, it would be easier to take this list of Mr. Montgomery's and see if they are in operation.

"Mr. Hatcher: We have analyzed the job orders. He testified that they do not reflect the actual condition.

"Mr. Garver: You have not made any effort to determine whether those units are in operation or not. If you are in doubt about it, go look at them and see.

"Mr. Stone: Mr. Black's inventory ought to show that, comparison would show it.

"Mr. Garver: Most of this stuff is units of compressor stations. He went to those stations and checked our inventory and used it.

"Mr. Hatcher: It would not show when it went in operation.

"Mr. Garver: It doesn't make any difference when it went in operation, if they were in operation September 1st.

"Commissioner Hill: Is it not a question of whether or not this property is used or useful upon the date September 1, 1931?

"Mr. Garver: That is it. Mr. Eastman's testimony is based his dates put in operation, if anybody doubts, let them go look at the property and not at the books.

"Commissioner Hill: We have a valuation upon the property as of that date, there seems to be some little question, but it does not seem to me it is material.

"Mr. Garver: There is no question between Mr. Black and Mr. Eastman, and because Mr. Black sent his men to the property and checked the property, we gave them the information they requested and if his men want to take the inventory and determine depreciation and to do that, they had to know the things were in operation and to determine the fact as to whether they were in operation or not, they could find out at the plant itself.

[fol. 594] "Mr. Hatcher: If ten or fifteen million dollars worth of this property was put in operation on September 1st, it was not there for the purpose of earning a return during the period covered by this investigation, and we would like to know what that property amounts to, if it was not there and available for earning during that period, it would distort our picture when we get to arriving at the property.

"Mr. Stone: Have you compared it with Mr. Black's inventory to see whether it is not included in the inventory?

"Mr. Hatcher: It is perhaps included. We want to know whether it was in operation. He cannot give us the date it went into operation.

"Mr. Stone: It don't make any difference, if it was in operation September 1st, at the time of the valuation.

"Mr. Hatcher: You cannot compare the value of September 1st, with earnings for September 30th.

"The Witness: The first item amounts to $237,000, approximately. B-12888 covers erection of two 1000 H. P. units, Moreland Compressor station. These were constructed and went into operation in the fall of 1930.

"Q. What month?

"A. I cannot tell you the exact month, I presume October or November. I know that they went into operation there

the winter of 1930. That covers both units, a total of $257,000. The next item amounts to $366,000, job order B-13889, three compressor units at Wichita. Those were installed some time about the same time as the Moreland units, in the fall of 1930, have been in operation ever since. The next item is $32,000, construct gas pipe line, Lyons, Kansas, to Nelson, Nebr. That line was constructed in the early part of 1930 and in 1931 and was in operation.

"Q. Do you know the month when the gas was first turned into that line?

"A. No, Mr. Black has in his possession some large maps which show the dates of construction of each one of these lines.

into Springfield, Mo., recently?

[fol. 395] "Q. Was there an extension of the line going

"A. No.

"Q. When was the last extension made on that line?

"A. Going into Springfield?

"Q. Into Missouri, the Sedalia line?

"A. There was an extension to that line.

"Q. When was the extension made to that line?

"A. Most of that, during the latter part of 1930 and the first part of 1931.

"Q. You don't know the time when the gas was put in that?

"A. There were several extensions made to the Sedalia line.

"Mr. Garver: Any items of lines in that Exhibit 88, the date of construction appears on Mr. Black's valuation, does it not?

"A. Yes, the next item of any importance is $151,000, purchase leases and wells in the Craig field, B-12845. Those leases and wells were purchased, approximately two years ago.

"Q. When was the gas turned into the field for storage purposes?

"A. A year ago this past fall. That would be in the fall of 1930.

"Mr. Stone: Do you mean a lease could not be charged to capital item until it began to produce?

"Mr. Hatcher: The thing I wanted to know is, when it was used in the system and began to affect the return.

"A. That particular field has been used in the system the last two years. The $20,000 item, I cannot say definitely whether that is the portion in Kansas or in Missouri.

"Q. What is that item?

"A. Construct gas pipe line from Ottawa, Kansas, to serve Missouri towns.

"Q. What is the job order?

"A. B-12828, amounting to $20,000.

"Q. You don't know the date?

"A. The line from Ottawa to Sedalia was constructed in the summer and fall of 1930.

"Q. The gas was turned in some time in the fall?

"A. Turned in in the fall of 1930. The next item, of any consequence, is $197,000, rearrange lines to compressor station near Drumright. That station was erected in the fall of 1930 and has been in operation since.

[fol. 596] "Q. What was the job order?

"A. B-12881. The next is $46,000, construct 32 miles of 20 inch line from Dilworth to South end of Wichita 16 inch line. That line was also constructed in 1930 and has been in operation ever since, B-12982. The next item is $87,000 install two 1000 H. P. Units, Higgins compressor station. Those units were installed the same time the units at Wichita, B-12893, installed in the summer and fall of 1930, have been in operation ever since. Item of $224,000, lay 34 miles of 6 inch line, 29 miles of 4-inch line, 12 miles of 3-inch line, 6 miles of 2-inch line, Carson County, Texas. I cannot identify the lines from this description here, B-12929. These lines were laid not later than the 1st of January, 1931.

"Q. All about the same date?

"A. They were all laid on the same job order, gathering lines to the wells in the Carson county field.

"Q. Will you give us the date when the gas was turned into the lines, that is, the approximate date?

"A. No, sir, I do not have any idea I could find the exact date the gas was turned into those lines. There would be no date kept of it. An item of 172,000, replace St. Joe 16-inch line between Lawrence and Tonganoxie, Kansas, B-12960. That work was delayed and was not completed, I believe, until this summer. However, it replaced a previously existing line. This is the cost of the new line: item of $43,000, install motor gas compressor at Ottawa station.

I cannot give you the date on that. It was at least prior to a year ago. There is an item of $49,000, drill and equip Freyler Well No. 2, Noble County, Okla. There has been an exhibit put in on that, it will give the job order and the information on that. There is an item of $32,000, job order B-13129, drill and equip Harris No. 1 well, Seminole County. I think the date of completion of that well would be shown in Mr. Black's valuation. These are the only items of any consequence in this list.

[fol. 597] "Q. Did you have any uncompleted construction of importance on September 1, 1931?

"A. We probably had some open job orders at that time.

"*A.* I am speaking now of the unfinished construction, property not in use?

"A. No, sir, no major items of construction were under way at that time.

"Q. Were there any wells drilled in 1931?

"A. I cannot say.

"Q. Can you tell us, Mr. Eastman, the amount of gas that has been stored in the Craig field?

"A. No, sir, I can tell you approximately, something in excess of a billion feet.

"Q. When was it put in?

"A. At various times during the last two years.

"Q. Have you used any of the storage gas from the Craig field?

"A. Yes, sir.

"Q. Do you know how much has been taken out?

"A. No, sir, in total, it is put in and taken out at different times throughout the year.

"Commissioner Hill: Mr. Eastman, I can see where it would be material if you spent, say, $2,000,000 in 1931 for new construction, for property being constructed, and only part of that became in use during that year if at the same time, you were asking a rate return upon that entire $2,000,000.00 for that year. I think that is the point, I guess you see that too. What we would like to know, if possible, is how much of that amount was used and useful during the year 1931?

"A. That is what I have tried to testify to, Mr. Hill. I can testify that practically all of it was used and useful during 1931 for this reason: In 1931 we have done scarcely

any construction work. The construction work was done during the year 1930.

"Commissioner Hill: Probably would not be $2,000,000.00 worth, there would be some, but you cannot tell us what amount that is?

[fol. 598] "A. I believe—I do not believe any of this $2,000,000.00 carried in this list of uncompleted job orders was—the work was actually done later than 1930. I have been able to identify all the larger amounts in here as to the year 1930. * * *"

"Mr. Hatcher: Our only purpose was to find out what property was not used and useful over the period covered by the investigation and affected by the return, and if the facts show the contrary evidence, we will do nothing. That is why I object to Mr. Hamilton's question.

"Mr. Stone: All of these items were shown to be used and useful in September, 1931, which is assumed to be the rate base. I wondered if you were merely going back for the purpose of income and outgo statements for 1930, or if you wish to take it from the general rate base.

"The Witness: May I answer that previous question? Included in this list is the cost of construction of Drumright station, Mr. Black has inventoried the Drumright station and deducted for accrued depreciation on both buildings and on the equipment.

"Mr. Hatcher: The only objection I had to Mr. Hamilton's question, he made an assumption which is not based on any fact, because we were simply trying to get at the actual condition that existed there, that is all, if it is there and used over the full period, it can be considered in the rate base.

"Mr. Stone: I was merely tryng to get at the purpose of the examination. I do not understand you quite answered my question, yet, on it.

"Mr. Hatcher: The only thing we had in mind was this. If there is property included in this rate base which was not used and not reflected in the return over that period covered, it should not be included so far as the rate of return is concerned.

[fol. 599] "Mr. Stone: Then it makes it quite important to put in, as we did yesterday, the income and outgo for the year 1931, if there would be any question about it being counted.

"Commissioner Hill: But having put that in, this other matter seems to be rather important as to whether all this property valued is used or useful over the period for 1931.

"Mr. Stone: This shows it was all in there a year and used and useful over the period for 1931, and therefore it was in the income and outgo in that statement of 1930, under Mr. Hatcher's theory.

"Commissioner Hill: As I see it, it is a question whether or not this $2,000,000 investment or expenditure for construction was in use during all of the year 1931. Now, under your amended exhibit, you show what your net earnings from operations were in 1931, for the entire year. You had a valuation of the date while it is really July 1st down to September 1st, now if this $2,000,000.00 is included in the valuation and a part was not in use during 1931, I can see where it would be material as to the amount not in use.

"Mr. Stone: This evidence shows, as shown here by this examination, all of it was in use all of the year 1931, except some, possibly some very minor items. That is why I was emphasizing that fact.

"Mr. Hatcher: That is why I cannot understand why you assume we are going to use it, if we get contrary information.

"Commissioner Hill: If the commission, at this time had to pass upon that proposition, we would be somewhat in the air, because we would have to say out of this $2,000,000.00, the evidence shows that a great amount or a big [fol. 690] part of it has been used and useful, or has been used during the year 1931, but we could not say specifically how much.

"Mr. Stone: Mr. Eastman's testimony goes to $1,678,000, which is shown to have been used during the whole year, 1931, out of the $2,000,000.00 and the others are minor items which may or may not, he is unable to testify to. I think that clarifies the situation. * * *"

[fol. 691] "No witness other than Eastman testified as to the matters covered by the above testimony.

"On rehearing, Eastman testified that all property included in Black's and Hamilton's valuation was in use during the entire year ending June 30, 1932.

"'In arriving at the average values the Commission took into consideration net additions to fixed capital from July 1,

1931, to September 1, 1931, amounting to $1,362,586, which is the total net additions shown on Exhibit 91 less the items of leaseholds and leasehold development costs shown thereon.

"The net additions from January 1, 1931, to June 30, 1934, taken into consideration by the Commission in arriving at the average values amounted to $777,591, which is the total of the additions during that period as shown by Exhibit 51, amounting to $993,970.59, less the items of leaseholds and leasehold development costs aggregating a net amount of $180,379.

"The net additions during the six months period ended December 30, 1930, and during the six months period ended June 30, 1931, are the net additions shown on Exhibit 51 covering those periods less the items of leaseholds and leasehold development costs.

"The item of leaseholds and leasehold development costs were omitted from the net additions because the leasehold values were added to the average values separately at the value found by the Commission, to wit: $2,274,200.00.

"The amount of uncompleted job orders was not deducted in any manner by the Commission in arriving at the average values.

"The book value of the plant and property of the company is included in two accounts, to wit: "Plant and Investment" and "Uncompleted Job Orders."

"The book value of the plant and property of the company including completed and uncompleted projects was as follows:

[fol. 6021] January 1, 1930:

| | |
|---|---|
| Plant and Investment Account | [illegible] |
| Uncompleted Job Orders | [illegible] |
| Total | [illegible] |

December 31, 1930:

| | |
|---|---|
| Plant and Investment Account | [illegible] |
| Uncompleted Job Orders | [illegible] |
| Total | [illegible] |

June 30, 1931:

| | |
|---|---|
| Plant and Investment Account | $96,795,538.93 |
| Uncompleted Job Orders | 2,208,457.57 |
| Total | $99,003,996.50 |

"The investment in plant and property increased during the six months period ended June 30, 1931, $238,532, and it increased during the twelve months period ended December 31, 1930, $11,675,447."

## Rate of Return

The following agreed statement is the evidence submitted to the District Court on the rate of return:

"Testimony in regard to a proper rate of return was given by the witnesses F. C. Hamilton, P. McDonald Biddison and Charles F. Clark for respondents and by C. H. Montgomery for the Commission.

"F. C. Hamilton is a member of the Executive Committee of Henry L. Doherty & Company and in charge of the Rate and Valuation Department of that company; P. McDonald Biddison is a gas engineer of national reputation who testified that he had had many years' experience in financing gas properties; Charles F. Clark, associated with Halsey Stuart & Company of Chicago, testified that he had spent practically his entire business life in intimate touch with the financial operations of the largest industries of the United States; C. H. Montgomery a certified public accountant of twenty years experience, had served for two years on the Kansas Public Service Commission, and from [fol. 603] his experience was familiar with financing matters.

"The witnesses Hamilton, Biddison and Clark, all testified that under existing economic conditions a fair rate should be in excess of 8% and that neither at this time nor in the immediate future could it be hoped that capital could be attracted to a project such as that of the Cities Service Gas Company for a return of 8% but that a much greater return would be required if capital could be interested at all.

"The witness Montgomery testified that a reasonable rate of return for the Cities Service Gas Company would be between 6% and 8% and further testified as follows:

"Q. You stated in your judgment 8 per cent was the amount in normal times that would interest capital?

A. A maximum of 8 per cent in normal times.

Q. Are times very abnormal now?

A. They are, very, at this time.

Q. Do you think you could interest capital in a project of this sort at 10 per cent now?

A. It might be difficult to interest capital under any conditions right at this time.

Q. Wouldn't you say, then that under present conditions 8 per cent would be the minimum?

A. If this project was being initiated at this time, it would be difficult. If such a proposition would be initiated under these conditions, it would be difficult to secure capital at a reasonable amount, if it was contemplated that these conditions would continue for an indefinite length of time.

Q. Well, suppose we are approaching this property as of September 1, 1931. Was the condition at that time any different than what it is now? Was the condition any different on September 1st, the date we have chosen for this reproduction, than it is now?

A. That would depend. Any change in condition probably has been for the worse.

Q. These financial experts have been seeing rainbows in the sky, have they not?

A. They are still seeing them in the future, but conditions have probably become worse since September 1st.

Q. Well, what do you say? Is 8 per cent as of September 1, 1931, an unreasonable rate of return?

A. If it was contemplated that those conditions would last indefinitely and if in view of those conditions anyone would have the courage to go out and embark on such an enterprise, they would probably expect to receive a higher rate than 8 per cent." • • •

[fol. 604] "Testimony was introduced to the effect that because of the assistance of the holding company, the Cities Service Company, the Cities Service Gas Company has been able to sell its securities at an 'interest rate that was from a half to three-fourths per cent less than anything else that was put out at about that time on a similar project,' and in addition to that it gets better terms on its mortgages. It

does not have to pay them off in ten years as many of the pipe line companies have had to do with issues that have been put out in the last two years. Because of this, the Cities Service Gas Company was able to sell its 5½ per cent bonds for 96¼.

'The company, having ample financial resources, does not necessarily have to issue securities now or six months from now, or two years from now. They pick and choose their time when the markets are right.'

"Montgomery's Exhibit 49 shows the financial history of the pipeline system under consideration beginning with the organization of the Cities Service Gas Company to date. The Cities Service Gas Company was organized in the latter part of 1926, acquiring the assets and assuming the liabilities of the following companies:

Empire Natural Gas Company.
Kansas Natural Gas Company.
Empire Gas and Pipe Line Company.
Kansas-Oklahoma Gas Company.
Empire Gas & Fuel Company (Delaware) (Gas properties only).

"The stock control of these companies had been theretofore acquired by Cities Service Company and their assets were acquired and liabilities assumed by the Cities Service Gas Company as of November 30, 1926. Balance sheets of the companies at the time of consolidation are shown on pages twenty-four and twenty-five of Montgomery's Exhibit 49.

[fol. 605] "These balance sheets show that at the date indicated the book value of the plant investment of the companies, including uncompleted job orders, was $52,182,525.98, and that reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95. These reserves which had been accumulated out of earnings amounted to 42.97 per cent of the plant investment.

"These balance sheets show that the companies had accumulated a surplus amounting to $14,903,660.21, which sum is equal to 87.26 per cent of the total capital stock of the companies taken over.

"The combined reserves for depreciation and depletion and surplus amounted to $37,327,597.16, which is equal to

218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment.

"In the case of the Empire Natural Gas Company, it had a capital stock of $10,574,000 and compared to such capital stock it had surplus of $6,066,436 and reserves for depreciation and depletion of $10,192,715, a total of surplus and reserves of $16,259,151, which is equal to 158.77 percent of its capital stock.

"The plant investment of the Empire Natural Gas Company, including uncompleted job orders, as reflected in the books of the company as of November 30, 1926, was $26,577,355; its reserves for depreciation and depletion amounted to $10,192,715, which is equal to 38.35 per cent of the plant investment.

"In the case of the Kansas Natural Gas Company it had a capital stock of $6,000,000 and surplus of $7,784,067 and had accumulated reserves for depreciation and depletion amounting to $11,905,381. Its surplus amounted to 129.73 per cent of its capital stock and the combined surplus and reserves amounted to 198.42 per cent of its capital stock. The book value of its plant investment was $18,861,223, including uncompleted job orders, and its reserves for depreciation and depletion of $11,905,381 was 63.12 per cent of such plant investment.

[fol. 606] "The Empire Gas and Pipe Line Company had a capital stock of $5,000 and surplus of $907,323, which was 18,146.46 per cent of its capital stock. Its reserve for depreciation and depletion was $325,840, making the combined reserves and surplus $1,233,163, all of which was accumulated on a capital stock of $5,000.

"The plant investment of the Empire Gas and Pipe Line Company, including uncompleted job orders, was $1,625,569, compared with combined surplus and reserves of $1,233,163.

"The financial history of the company since the consolidation in November, 1926, may be found on pages 1 to 8, inclusive, in Exhibit 49, which reflects the combined operations of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company and the American Pipe Line Company.

"It is shown there that surplus has been accumulated, in excess of all interest and dividends paid, of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have

increased to $10,818,020. Its total assets have increased from $60,595,001 as of December 31, 1926, to $100,431,039 as of June 30, 1931.

"The Cities Service Gas Company has during all this time paid interest on its bonds and dividends on its capital stock; in 1928 it paid $1,000,000 dividends, and in 1929 and 1930 it paid $2,000,000 each on dividends, which is at the rate of 8 per cent per annum. Its earnings before interest and depreciation were as follows:

| | |
|---|---|
| 1927 | $5,330,739 |
| 1928 | 6,053,021 |
| 1929 | 8,000,702 |
| 1930 | 8,899,480 |
| Twelve months ending June 30, 1931 | 8,741,809 |

"The net profit of the companies, after paying all interest charges available for reserves and common stock during each of the years 1927 to 1930, was:

[fol. 607]

| | |
|---|---|
| 1927 | 14.00% |
| 1928 | 13.12% |
| 1929 | 21.26% |
| 1930 | 19.07% |

"Its net return after paying all interest and other charges and providing substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

| | |
|---|---|
| 1927 | 9.06% |
| 1928 | 6.75% |
| 1929 | 14.53% |
| 1930 | 10.82% |

"Page 1 of Exhibit 49 shows that the book value of plant investment, including uncompleted job orders, increased from $53,243,128 as of December 31, 1926, to $99,003,996 as of June 30, 1931, an increase of $45,760,868."

Exhibit 49 introduced by Montgomery for the Commission shows that the book value of the plant investment account represents the value at which the property of the company was placed on its books at the time of the con-

solidation in 1926 plus net additions since that time. The value at which the property was placed on the books in 1926 was the aggregate of the book value of the respective properties consolidated including the property of the Kansas Natural Gas Company. The annual reports of the Kansas Natural Gas Company filed with the Department of State of the State of Kansas for the years ending December 31, 1921 introduced as Exhibit 8 and December 31, 1922, introduced as Exhibit 9, show the resources, liabilities, capital and reserves of this company at the above stated dates as follows:

| | December 31, 1921 | December 31, 1922 |
|---|---|---|
| Total Resources | $12,922,834.61 | $23,443,210.00 |
| Liabilities | 1,785,551.21 | 2,572,838.63 |
| Capital Stock | 7,700,250.00 | 6,000,000.00 |
| Surplus | 748,522.54 | 1,568,243.84 |
| Reserves | 2,687,510.86 | 13,302,128.53 |
| Total Liabilities, Capital and Reserves | $12,922,834.61 | $23,443,210.00 |

[fol. 608] "Total Resources" includes the book value of plant investment which was $11,241,229.97, at December 31, 1921 and $20,389,857.72 at December 31, 1922, an increase of $9,148,627.75.

No new capital was paid in; the combined capital and surplus was less at December 31, 1922 than it was at December 31, 1921.

Hypothetical Pipe Line

"George I. Rhodes testified that he was vice-president and chief engineer of Ford, Bacon & Davis, Inc., a nationally known firm of engineers with headquarters in New York and principal office in Philadelphia, Cleveland, Chicago and San Francisco and offices through which properties are managed in Monroe, Louisiana, Amarillo, Texas, and Colorado Springs, Colorado; that he graduated from Massachusetts Institute of Technology in 1905, and has been continuously engaged in engineering work ever since; that he is familiar with the construction of gas pipe lines and has been engaged in the designing and construction of

such lines for approximately eight years, such work including examination of properties and proposed projects both as to pipe lines and gas reserves; that he was employed by Hamilton and Creveling (of Henry L. Doherty & Company) to make an estimate of the money that would be required to construct a pipe line to take gas solely from the Amarillo field and deliver it to the wholesale delivery points now served by the Cities Service Gas Company and allied companies and also to estimate the amount and cost of gas reserves in connection therewith; that the gas reserves were purely hypothetical "because none of us had any idea that the requisite amount of gas could at this time be purchased and it was therefore necessary to assume that the amount of available acreage in the field would be great enough so that a reasonable reserve—that a purchase of [fol. 609] required reserves could be made without cornering the market, so to speak"; that the proposed hypothetical pipe line is shown by Exhibit 13, a map with the lines projected thereon; that Exhibit 14 is a report showing the estimated cost; that the lines are platted "as the crow flies, rather than taking the actual topography into consideration"; that the lines have been designed as cheaply as could be done; that the quality of service has been reduced from that of the present system; that the system was designed to make an aggregate delivery of approximately 325,000,000 cubic feet of gas per day maximum; "we considered that it would require a reserve of 250,000 acres which we assumed would be pretty well scattered over the field with a correspondingly large gathering system"; * * * "We estimated that the total amount of funds required to acquire the reserves and construct and put the system into operation would be $91,500,000."

"On cross-examination the witness testified that the hypothetical system is comparable to the present system in that it will serve the same markets; that no check of the present system was made to find out whether it had more or less capacity; that the hypothetical system differs in that it has a single source of supply and that a larger number of towns are served with but a single line to them; that the hypothetical system is "somewhat less than the equipment of the present system"; that no consideration was given to gas supplies in Kansas and Oklahoma; that in de-

signing an actual project any available gas closer than Texas would be taken into consideration; that the witness did not attempt to design a project contemplating any supply of gas from Kansas or Oklahoma and could not estimate the difference in price without refiguring the entire project; that the witness is familiar with gas lease prices but is prohibited from testifying in that regard on account [fol. 610] of commitments to other clients; that 250,000 acres of leases could not be bought in Texas at the present time; that $11,000,000.00 was estimated as the probable cost of 250,000 acres or $44.00 an acre. The witness testified that he had no personal knowledge of company's present pipe line system.

Exhibit 14 by Ford, Bacon & Davis, as to cost of hypothetical pipe line introduced by the Company is as follows:

"As requested we have briefly investigated a suggested natural gas system to produce gas solely in the Amarillo Gas Field and to transport and deliver it economically and dependably to the wholesale delivery points and city gates to which gas is now being delivered by the system of the Cities Service Gas Company.

"We have designated such a system having the following characteristics and normal estimated costs:

| | |
|---|---|
| Present Net Daily Delivery Capacity which can be extended as required to meet growth of the system | 325,000 M c. f. |
| Annual Delivery at present capacity and current seasonal variations in demand | 78,600,000 M c. f. |
| Preconstruction and Organization Cost including engineering and geological investigations and reports on economics and stability of project, earning capacity, etc., the organization of a Company to carry out the project and the negotiation of basic contracts necessary to have in hand before considering the financing of the project | $1,250,000 |
| Financing Cost exclusive of discount on securities but including the cost of negotiations, preparation of extensive financing reports, cost of legal expenses, taxes, etc. involved in the issuance of securities | 250,000 |

| | |
|---|---|
| Gas Reserves sufficient to insure at least a 20 years' supply of gas with reasonable growth in load taken at a conservative estimate of the gas content of acreage. 250,000 acres minimum in proven territory | 11,000,000 |
| [fol. 611] Gas Wells fully equipped, sufficient in number to supply and measure the maximum daily requirement and to protect acreage from migration of gas. 150 producing wells | 5,000,000 |
| Gathering System from all wells to a centrally located field compressing station comprising lines from 4 inches to 24 inches in diameter. 272 miles | 3,530,000 |
| Gasoline Plant sufficient to strip 325,000 M. F. C. of gas daily with 1,500,000 gal. storage and laid out for convenient extension | 600,000 |
| Field Compressing Station sufficient in capacity to compress gas from 200 pounds to 450 pounds gauge and to minimize in the compressed gas all moisture that can condense in the lines, the station having normal spare capacity. $17,500 horsepower | 1,870,000 |
| Main Pipe Lines comprising two parallel inter-connected lines 24 inches as far as Wichita Junction, thence 22 inches to Kansas City, the double lines being required to give service approaching that possible with the present system with its multiple lines and sources of gas. 920 miles of pipe | 29,310,000 |
| Five Main Line Compressing Stations to repressure the gas in the lines to 450 pounds as required to transport the maximum requirements of gas through the main line, each station having normal spare capacity. 51,250 horsepower | 5,210,000 |

| | |
|---|---|
| Branch Pipe Lines from 2 inches to 20 inches in diameter to reach the various wholesale points of delivery and city gates, each line having sufficient capacity to meet reasonable expectation of growth in demand. | |
| 2,024 miles | 17,630,000 |
| 235 Regulator and Meter Stations at points of wholesale delivery and city gates | 1,060,000 |
| [fol. 612] Telephone System connecting the field with all compressing stations and principal wholesale delivery points, comprising two circuits along the main line and a single circuit along major branch lines. | |
| 1,735 miles of circuit | 730,000 |
| Miscellaneous Property comprising shops, warehouses, garage, automotive equipment, maintenance and repair equipment and other miscellaneous items of property | 1,520,000 |
| Engineering and Supervision Costs including preparation of detail designs and specifications, negotiations for purchase of materials and equipment and for construction contracts, inspection and supervision of manufacture of materials and of construction work | 3,870,000 |
| Interest During Construction based on a 24 months' construction period | 5,060,000 |
| Taxes, Insurance and Other Corporate Overheads during the construction period | 2,110,000 |
| Working Capital | 1,500,000 |
| Estimated Total amount of funds required to acquire reserves and to construct and put the system into operation | $91,500,000 |

We hand you herewith a map showing the suggested system, with the following title:

"Cities Service Gas Company. A suggested natural gas system to produce gas in the Amarillo gas field alone and to deliver the gas to present wholesale delivery points."

This map shows the suggested extent of acreage and number of wells required in the Amarillo Gas Field, the suggested location, size and number of pipe lines, the suggested location, size and number of compressing stations and the approximate location of the principal whole-sale points of delivery.

A further investigation and consideration of the suggested system might be expected to refine its design, to adapt it more specifically for the service now possible from the system of the Cities Service Gas Company, to support the estimates of cost with confirming data and details and [fol. 613] to supplement them with estimates of the cost of gas delivered.

## Intercorporate Relations

The following agreed statement as to intercorporate relations was presented to the District Court:

"Henry L. Doherty owns over 35 per cent of the voting power of the Cities Service Company and with two exceptions the rest of the stock is in the hands of scattered individuals.

"The common stock of the following distributing companies, respondents herein, is owned by the Gas Service Company with the exception of the qualifying directors' shares: Arkansas Valley Gas Company, Capital Gas and Electric Company, Girard Gas Company, Hutchinson Gas Company, Newton Gas Company, Union Public Service Company, Pittsburg Gas Company, Western Distributing Company, Wichita Gas Company, and Wyandotte County Gas Company.

"The common stock of the Cities Service Gas Company, which sells the gas at the city gates to distributing companies now under investigation, with the exception of directors' shares, is owned by the Empire Gas & Fuel Company. All of the voting stock, with the exception of the directors' shares of the Empire Gas & Fuel Company is owned by the Cities Service Company.

"All of the stock of the Cities Service Gas Pipe Line Company, except qualifying directors' shares, is owned by the Cities Service Company.

"All of the stock, except qualifying directors' shares, of the American Pipe Line Company is owned by the Cities Service Gas Company."

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[fol. 614] STIPULATION AS TO CONDENSED STATEMENT OF EVIDENCE

The parties to the above entitled action, by their respective attorneys, stipulate and agree that the foregoing is a true and correct condensed statement of all the evidence introduced before the court in the trial of said action, material to the issues presented on appeal.

This 5th day of May, 1933.

Chas. D. Welch, Louis R. Gates, Chas. W. Steiger, Roland Boynton, Atty. General; E. H. Hatcher, Attorneys for Appellants. Robt. D. Garver, Robert Stone, Attorneys for Appellees.

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[fol. 615] IN UNITED STATES DISTRICT COURT

ORDER APPROVING CONDENSED STATEMENT OF EVIDENCE

The foregoing condensed statement of the evidence introduced before this court, having been stipulated by counsel for the respective parties to be correct, the same is hereby approved and settled as correct this 15th day of May, 1933.

Orie L. Phillips, Geo. T. McDermott, Circuit Judges.
Richard J. Hopkins, District Judge.

[File endorsement omitted.]

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[fol. 616] IN UNITED STATES DISTRICT COURT

PRÆCIPE FOR TRANSCRIPT OF RECORD—Filed May 15, 1933

To the Honorable F. L. Campbell, Clerk District Court of the United States for the District of Kansas, First Division;

In the certified transcript of the record in the above entitled cause to be made and transmitted to the Supreme

Court of the United States pursuant to an order allowing appeal, dated April 19, 1933, signed by Orie L. Phillips and George T. McDermott, Circuit Judges, and Richard J. Hopkins, District Judge, kindly incorporate the following:

1. Bill of Complaint for injunction filed by the Wichita Gas Company, No. 1637 N, and all exhibits attached thereto including the opinion and orders of the Public Service Commission for the State of Kansas; and the Bill of Complaint for injunction filed by the Cities Service Gas Company, No. 1646 N. All other petitions in the consolidated cases are similar in form and need not be included;

2. Answer filed by defendants in answer to the petition filed by the Wichita Gas Company, No. 1637 N, and the Cities Service Gas Company, No. 1646 N;

3. Request for convening of three judge court;

4. Order consolidating cases;

5. Opinion and findings of the District Court and supplemental memorandum;

6. Dissenting opinion and findings of Hon. Richard J. Hopkins, District Judge;

7. Final decree, or order of the District Court;

[fol. 617] 8. Order substituting parties defendant;

9. Appellant's petition for appeal to the United States Supreme Court, assignment of errors and prayer for reversal;

10. Jurisdictional statement;

11. Order allowing appeal;

12. Copy of bond on appeal;

13. Citation to appellees with return thereon;

14. Acknowledgement of service of appeal papers;

15. Condensed statement of the evidence;

16. This praecipe.

Chas. D. Welch, Louis R. Gates, Chas. W. Stoiger, Roland Boynton, Atty. General; E. H. Hatcher, Attorneys for Appellants.

Received copy of the foregoing praecipe this 5th day of May, 1933.

By Robt. D. Garver, Robert Stone, Attorneys for Appellees.

[File endorsement omitted.]

[fol. 618] Clerk's certificate to foregoing transcript omitted in printing.

[fols. 619 & 620] In United States District Court

[Title omitted.]

[fol. 621] Order Extending Time to File Transcript of Record on Appeal. Filed in U. S. Supreme Court May 26, 1933

For good cause shown, it is by the Court ordered that the time for filing transcript of record on appeal in the Supreme Court of the United States in the above entitled causes, be and the same is hereby extended for a period of thirty days from and after May 29, 1933.

Geo. T. McDermott, Circuit Judge.

[fol. 621½] [File endorsement omitted.]

[fols. 622 & 623] In Supreme Court of the United States

[fols. 624 & 625] Statement of Points to be Relied upon and Designation of the Parts of the Record to be Printed. Filed May 31, 1933

Come now the appellants and adopt their assignments of error as their statement of points to be relied upon, and represent that the whole of the record as filed is necessary for the consideration of the case.

Chas. H. Welch, Louis R. Oates, Chas. W. Steiger, Roland Boynton, Atty. General; E. H. Hatcher, Counsel for Appellants.

Service of copy of the above notice is hereby acknowledged this 27 day of May, 1933.

Robert D. Garver, Robert Stone, Counsel for Appellees.

[fol. 626] [File endorsement omitted.]

Endorsed on cover: File No. 37,717. Kansas D. C. U. S. Term No. 114. The State Corporation Commission for the State of Kansas, Homer Hoch, Jesse W. Greenleaf, et al., appellants, vs. The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, et al. Filed May 31, 1933. File No. 114, O. T., 1933.

(4080)